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1915, Section 623**

A STRONG RECOVERY

Yes, it's possible.

The conventional wisdom says the end of recession will bring only a weak economic recovery. That may be, for there are plenty of problems left—from high debt to weak banks. But the economy just may give us all a pleasant surprise. Here's why.

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While other companies are working furiously to sell you an open system, we would like to offer you something with even greater promise.

The Open Advantage. Three words that represent an unequalled commitment to open systems, open computing and open networking.

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The Open Advantage starts with Network Application Support (NAS), a comprehensive implementation of standards that actually enables you to integrate applications across a multi-vendor networked environment, protecting them from the differences between manufacturers.

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There's virtually nothing we won't do to solve your problems.

solutions from whatever companies offer them and make them work with both

THERE'S AN OPEN ADVANTAGE TO DOING BUSINESS WITH DIGITAL.

NAS FROM DIGITAL

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not only files and data, but applications.

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With NAS you can open almost any computing environment.



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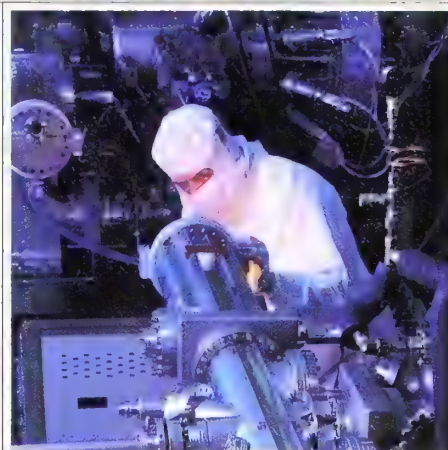
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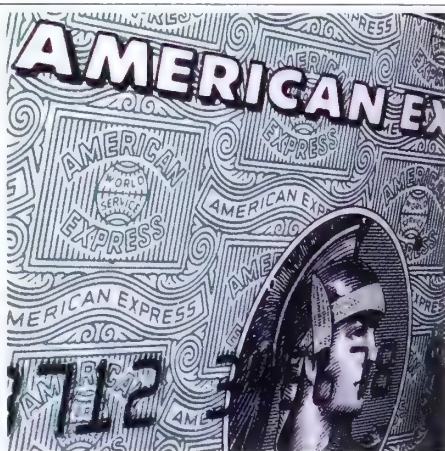
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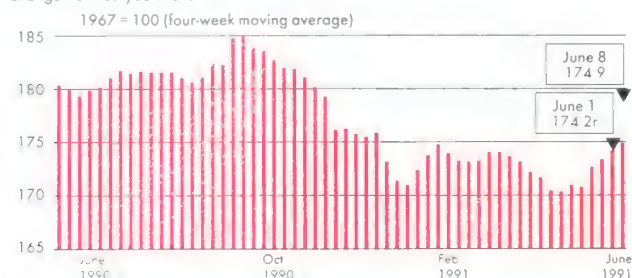
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The Fed's best move is no move
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BusinessWeek Index

PRODUCTION

Change from last week: 0.4%

Change from last year: -2.8%



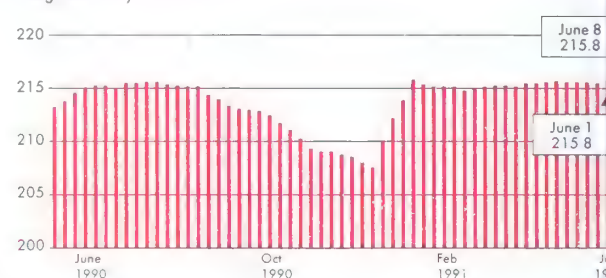
The production index increased for the week ended June 8. On a seasonally adjusted basis, rail-freight traffic and the output of trucks, steel, coal, paperboard, paper, and lumber rose. Electric power output was down sharply, and auto production also dropped, while the crude-oil refining output was unchanged from the previous week. Prior to calculation of the four-week moving average, the index declined to 174.3, from 175.5 in the week before.

BW production index copyright 1991 by McGraw-Hill Inc.

LEADING

Change from last week: 0.0%

Change from last year: 0.3%



The leading index was little changed for the week ended June 8. Slight lower stock prices, higher long-term bond yields, and slower growth rates for real estate loans and money supply offset the positive signs of a smaller rate of decline in the prices of industrial materials and a moderate drop in the number of business failures. Before calculation of the four-week moving average, the index fell to 215.8 from 216.7 in the previous week.

Leading index copyright 1991 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (6/15) thous. of net tons	1,630	1,551#	-13.4
AUTOS (6/15) units	118,950	110,345r#	-17.7
TRUCKS (6/15) units	79,326	79,807r#	-14.8
ELECTRIC POWER (6/15) millions of kilowatt-hours	60,055	57,871#	1.6
CRUDE-OIL REFINING (6/15) thous. of bbl./day	14,001	13,758#	3.4
COAL (6/8) thous. of net tons	19,097#	16,345	-6.8
PAPERBOARD (6/8) thous. of tons	759.6#	749.4r	-1.0
PAPER (6/8) thous. of tons	734.0#	735.0r	-1.9
LUMBER (6/8) millions of ft.	537.3#	438.2	5.5
RAIL FREIGHT (6/8) billions of ton-miles	19.0#	16.5	-8.2

Sources: American Iron & Steel Inst., Ward's Automotive Reports, Edison Electric Inst., American Petroleum Inst., Energy Dept., American Paper Inst., WWP, SFP, Association of American Railroads

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (6/19)	140	142	155
GERMAN MARK (6/19)	1.79	1.79	1.68
BRITISH POUND (6/19)	1.63	1.65	1.72
FRENCH FRANC (6/19)	6.10	6.06	5.64
CANADIAN DOLLAR (6/19)	1.14	1.14	1.18
SWISS FRANC (6/19)	1.54	1.53	1.42
MEXICAN PESO (6/19)	3,002	3,001	2,852

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound expressed in dollars.

PRICES

	Latest week	Week ago	% Change year ago
GOLD (6/19) \$/troy oz	367.400	372.000	5.9
STEEL SCRAP (6/18) #1 heavy, \$/ton	89.00	89.00	-22.3
FOODSTUFFS (6/17) index, 1967=100	199.9	201.4	-11.0
COPPER (6/15) ¢/lb.	103.8	103.3	-11.2
ALUMINUM (6/15) ¢/lb.	58.5	56.5	-20.7
WHEAT (6/15) #2 hard, \$/bu.	3.02	3.02	-17.3
COTTON (6/15) strict low middling 1-1/16 in., ¢/lb.	79.31	79.86	5.0

Sources: London Wed. final setting, Chicago mkt., Commodity Research Bureau, Metals Week, Kansas City mkt., Memphis mkt.

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (6/14) S&P 500	375.25	384.99	7.8
CORPORATE BOND YIELD, Aaa (6/14)	9.01%	8.93%	-2.1
INDUSTRIAL MATERIALS PRICES (6/14)	98.4	97.9	-5.1
BUSINESS FAILURES (6/7)	359	397	15.3
REAL ESTATE LOANS (6/5) billions	\$404.5	\$404.8	5.1
MONEY SUPPLY, M2 (6/3) billions	\$3,385.0	\$3,386.3r	3.1
INITIAL CLAIMS, UNEMPLOYMENT (6/1) thous.	401	439	12.2

Sources: Standard & Poors, Moodys, Journal of Commerce (index: 1980=100), Dun & Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. CIBC seasonally adjusts data on business failures and real estate loans.

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
INDUSTRIAL PRODUCTION (May) total index	105.8	105.3r	1.1
CAPACITY UTILIZATION (May)	78.7%	78.5%r	-5.1
CONSUMER PRICE INDEX (May)	135.6	135.2	0.0
PRODUCER PRICE INDEX (May) finished goods	121.8	121.1	0.3

Sources: Federal Reserve Board, BLS

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (6/3)	\$850.6	\$851.9r	1.1
BANKS' BUSINESS LOANS (6/5)	312.0	312.4r	-0.1
FREE RESERVES (6/12)	540	865r	NM
NONFINANCIAL COMMERCIAL PAPER (6/5)	148.9	148.4	0.0

Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed for two-week period in millions)

MONEY MARKET RATES

	Latest week	Week ago	% Change year ago
FEDERAL FUNDS (6/18)	5.82%	5.79%	8.28
PRIME (6/19)	8.50	8.50	10.00
COMMERCIAL PAPER 3-MONTH (6/18)	6.11	6.15	8.16
CERTIFICATES OF DEPOSIT 3-MONTH (6/19)	6.04	6.11	8.24
EURODOLLAR 3-MONTH (6/15)	6.13	6.06	8.21

Sources: Federal Reserve Board, First Boston

*Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

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ONE THAT GOT AWAY FROM LEXUS AND INFINITI

An MBA from a top-ranked school, management position with a medical-diagnostics company, car allowance, married, two children, thirtysomething, owner of a German sedan, neatly dressed, etc., I would seem to fit most of the demographics that cars made by these companies are aimed at ("Who's the most pampered motorist of all?" Marketing, June 10). But after visiting one Infiniti and two Lexus dealerships in the Philadelphia area, I was disappointed that no salesperson approached me for a personal introduction and offered to help me. Even after I struck up conversations about the features of the cars, no test drive or product information was offered. I don't recall anyone asking my name or giving me their business card. If an unmowed lawn cost a dealership \$2,500 after a visit by a mystery shopper, I wonder what the company penalty is for the shabby treatment I received. (I have since purchased a different European sedan.)

By the way, it would be interesting to see how many of Infiniti's mystery shoppers are African-American.

Kevin Brown
East Norriton, Pa.

WHY ALL THE FUSS ABOUT THE JAPANESE IN EUROPE?

Your otherwise informative article "The battle for Europe" (Cover Story, June 3) was marred by not-so-subtle Japanophobia ("Suddenly, there's a danger that some critical European industries will be hollowed out"; "Japan's strong presence is putting a heavy damper on the Europhoria of 1992"). A quarter-century ago, Europeans feared the U.S. juggernaut. Remember *Le Défi Américain* [*The American Challenge*]? But we taught them how to manage better, make better use of assets, and raise productivity. There's no reason for Europeans to expect any less of the Japanese, nor should we.

Robert B. Reich
Harvard University
Cambridge, Mass.

I found your report to be informative yet quite unfair to the Japanese presence in the region.

American companies have been spending heavily in Europe for years, and European corporations hold an enormous amount of investment in U.S. industries. Why should Japan be criticized for similar actions?

The war overtones throughout the piece particularly disturbed me and seemed to represent global distrust, not economic cooperation. Joint ventures, technology-sharing, and other free-market arrangements represent progress and teamwork, not animosity and domination.

As a student who has lived, studied, and worked abroad, I feel that the recent escalation of overall investment in Europe by U.S. and Japanese—in addition to European—corporations is a positive sign that will end up adding to global understanding and cooperation, as well as profits, for the world's three major economic regions.

Andrew Darlow
Colonia, N.J.

DOW CORNING: KEEPING AN EYE ON SILICONE RISKS

In "Breast implants: What did the industry know, and when?" (Legal Affairs, June 10), BUSINESS WEEK's omission of Dow Corning's ongoing disclosure of public health information only serves to continue public confusion on this important issue. You also omitted commentary from the medical community—particularly distressing given its role as the primary provider of information about the benefits and risks of this surgery for women.

Dow Corning has provided information to the medical community regarding our breast-implant studies ever since that community asked us to enter the marketplace in 1963. We continue this practice today.

Dow Corning continues to inform the Food & Drug Administration on the status and results of our ongoing research. Of particular interest have been the results of studies reported voluntarily by

BUSINESS WEEK
JULY 1, 1991 *** 3220
ISSN 0007-7135



Published weekly, except for one issue in January, by McGraw-Hill, Inc., Executive, Editorial, Circulation, and Advertising Offices, McGraw-Hill Building, 1221 Avenue of the Americas, New York, N.Y. 10020. Telephone: (212) 512-2000. Domestic Telex: 12-7960; International Telex: 232365. Cable: McGraw-Hill, New York. TWX: 710-611-1879. U.S. subscription rate \$39.95 per year; 2 years, \$69.95; 3 years, \$94.95. Single copies, \$2. Write for rates in other countries. Business Week Subscriber Services: 1-800-635-1200.

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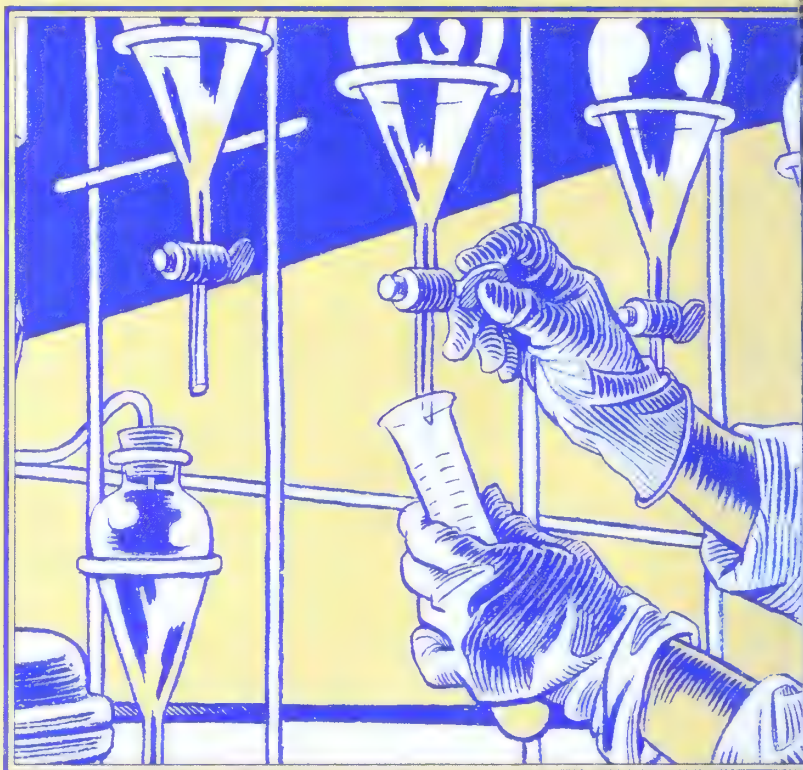
DIGITAL OPENS COMPANY WITH STRONG

It was a task no less formidable than developing a new drug and bringing it to market. We had to be creative. Persistent. Utterly dedicated to our goal.

That goal was to bring truly open computing to pharmaceutical companies. By using our Network Application Support (NAS) Environment for Manufacturing to integrate departments as diverse as R&D, Quality Control and Production. So people can work together to develop new products, get them approved and into the market in less time than ever before.

The NAS Environment does so by integrating different applications as well as different computers. And giving users the means to access data wherever it resides, then work with that data in their own applications.

Products and services based on industry standards are the key. With them, NAS unites Digital systems, IBM



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Readers Report

Dow Corning to the FDA concerning gels implanted in laboratory rats.

In the FDA's words: "Experts concluded (a) that the results of the rat study are unlikely to apply to humans; (b) that although a risk from silicone breast implants cannot be completely ruled out, there are at present no convincing animal or human studies that point to such a risk; and (c) that if a cancer risk does exist from silicone breast implants, it would be very small."

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J. Kermit Campbell
Group Vice-President, U. S. Operations
Dow Corning Corp.
Midland, Mich.

IF YOU HAVE A FAX, DO YOU NEED A SCANNER?

I enjoyed your article "Let your PC do the faxing" (Personal Business, June 3). But, regarding the last paragraph

about adding a scanner to your PC, I thought I'd point out something that many people don't realize: If you have a fax card and a fax machine, you can use the fax itself as a scanner. Simply "transmit" the document from your fax into the PC, and it's ready to forward to others.

I have found this to be a handy way to store copies of articles, clippings, etc. Most good fax boards come with compression software that stores fax documents in less space than a page of typed text. Sometimes, you have to make it a full-time job to keep up with this stuff. (I do.)

Bob Lambert
Vice-President
New Technology & Development
Walt Disney Pictures & Television
Burbank, Calif.

You do your readers a great injustice by telling them that "It takes only a few minutes and a screwdriver to take off a computer cover and slip a board inside." Your writer should be required to install one of these boards to experience all the snags that one can run into, from running out of memory to conflicts with existing programs. It can require

days to untangle these conflicts and arrange how programs are called to the fax board to work.

Henry P. Dair
President
Aline Systems Co.
Santa Fe Springs, Calif.

A DRACONIAN PROPOSAL FOR AMERICA'S ILLS

Of course liberal totalitarians find that any policy they support deserves financial backing from Washington ("Why business needs a stronger and wiser—Uncle Sam," Economic Viewpoint, June 3). Then, when educating health care, banking, or transportation "fail" to match some magic criteria, their solution is more government power, more tax money, and more restrictions on an individual's property or personal rights. Lament the level of resources wasted on and by Washington, but don't try to make us believe that other systems work better because their citizens have fewer and weaker personal freedoms (the truth behind "stronger government"). "Failing" sectors under our system are those where government involvement has been too

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longest. Cut total government spending to 20% of GNP for all levels, and our weaknesses will be difficult to spot through the surrounding prosperity.

Robert W. Hughes
Houston

NOT COST-BASED FEES THAT WOULD FAVOR AT&T

In "The little guys of long distance are mighty nervous" (Top of the News, June 3), you portray a study commissioned by us as concluding that smaller carriers would suffer a tremendous cost advantage relative to AT&T "if cost-based fees are allowed." In fact, a central finding of that study—confirmed by several of the regional Bell companies—that the old FCC rules would not result in "cost-based fees" but would give AT&T a huge and undeserved cost advantage. Smaller long-distance carriers support cost-based fees for local access. Thus, we are urging the FCC to maintain "equal charge" pricing until it undertakes a comprehensive review to determine the most equitable, cost-based formula for the 1990s and beyond.

James M. Smith
President
Competitive Telecommunications Assn.
Washington

CORRECTIONS & CLARIFICATIONS

In a recent story, "Suddenly, Asian-Americans are a marketer's dream" (Marketing, June 17), BUSINESS WEEK misidentified Caroline Pisaniello. She is a senior consultant at Deloitte & Touche.

REMY: THERE'S NO CHINESE PRISON LABOR BEHIND DYNASTY'S GRAPES

I would like to clarify statements attributed to an official of Remy et Associés, our French parent company in your article "China's ugly export secret: Prison labor," (International Business, Apr. 22).

Remy became aware that small quantities of the grapes that were provided by one supplier (among 36) to our Chinese partner came from a prison camp. Remy immediately objected and was assured by our Chinese partner that all purchases from that supplier would be discontinued.

Subsequently, at Remy's request, the company's Chinese partner agreed to set up a procedure to verify, before acceptance, the origin of each and every lot of grapes delivered to the winery. We have

confidence in the effectiveness of this screening process. We know for a fact that since 1987, there has not been a single instance of grapes from a labor camp being used in the production of Dynasty.

Gijs Hooft Graafland
Chairman & President
Remy Amerique Inc.
New York

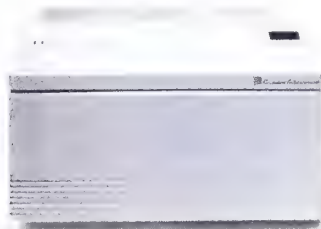
A HOT-GROWTH COMPANY DEFINES ITS MISSION

Universal International Inc. takes pride in being ranked 39th-best-performing small corporation in America ("Hot growth companies," Cover Story, May 27). But we would like to clarify our description: Universal is one of the nation's oldest and largest closeout wholesalers. We purchase, warehouse, and distribute excess inventories into the secondary marketplace.

Norman Ravich, Chairman
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New Hope, Minn.

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LIGHT SUMMER READS THAT WON'T LEAVE YOU HUNGRY

The ideal vacation book, humorist Dave Barry once observed, is one the critics have hailed as "waterproof." Given the crimp this would put in your reading list, however, I say settle for paperbacks. Why wear a hole in your beachbag? But just because a book is lightweight doesn't mean that what's inside has to be. Here's a selection of good reads, now out in softcover, about business, politics, foreign affairs—and yes, escape.

Barbarians at the Gate: The Fall of RJR Nabisco by Bryan Burrough and John Helyar (Harper Perennial, \$10.95). During 1988-89, the \$28 billion takeover of RJR Nabisco entangled every major investment bank and law firm on Wall Street. *Barbarians* puts readers in the middle of the action, offers marvelous portraits of the key characters, and opens a window on the Street's sometimes startling ways. One overriding impression lingers: Ego quickly overpowered greed as the contest's driving force.

Father, Son & Co.: My Life at IBM and Beyond by Thomas J. Watson Jr. and Peter Petre (Bantam, \$5.99). During Watson's 1956 to 1971 tenure as CEO, IBM grew from a \$735 million tabulating-machine maker into a \$7.5 billion computer giant. But this is less a business book than a casual, meandering memoir. Most fascinating is the author's harsh portrait of his father. Watson Sr., he writes, drove out IBM's ablest executives, surrounded himself with yes-men, and failed to grasp the significance of the computer age. Father and son fought constantly, about almost everything.

The House of Morgan: An American Banking Dynasty and the Rise of Modern Finance by Ron Chernow (Touchstone, \$14.95). Chernow's monumental history, winner of a National Book Award, offers a remarkable blend of scholarship and readability. While Chernow does yeoman work explaining the current state of affairs at 60 Wall St., the heart of his rich, well-documented book is in effect, a pair of biographies, of J.P.

Morgan Sr. and Jr. We learn as much about the times in which they lived as about these resolute men.

Gene Dreams: Wall Street, Academia, and the Rise of Biotechnology by Robert Teitelman (BasicBooks, \$10.95). An editor at *Institutional Investor*, Teitelman has fashioned an intriguing tale of the hype and bluster behind the gee-whiz biotech biz. He tells the story through the lens of an entrepreneurial hopeful, Genetic Systems. Drama and dreams, greed and false expectations fill this account of Wall Street's mad search for companies offering miracle cures.



A Random Walk Down Wall Street: Updated for the 1990s Investor by Burton G. Malkiel (Norton, \$14.95). For novices, this is a top-notch introduction to the financial markets and personal money management. For those with a finance background, it's a clear and enjoyable excursion through the latest research on the markets. This, the 5th edition, covers the 1987 crash and looks ahead into the '90s. A Princeton economics professor, Malkiel offers lively prose and telling analogies. You'll learn a lot, but you won't feel you're working.

Inside Job: The Looting of America's Savings and Loans by Stephen Pizzo, Mary Fricker, and Paul Muolo (Harper Perennial, \$10.95). This account of the S&L industry's decline is studded with murder, arson, bribery, and sex. The players include politicians, hit men, homebuilders, high rollers, and hookers. All, say the authors, had a hand in the

thrifts' downfall. The book shows how personalities and circumstances converged to make the looting possible. The paperback has been updated.

The Death of the Organization Man by Amanda Bennett (Touchstone, \$9.95). The jacket makes this seem like a "how-to-survive-a-downsizing" guide. Actually, it's a concise history of Corporate America as seen through the fate of its mid-level managers, whose ranks were decimated by layoffs in the '70s and '80s. There's poignancy in the stories of these corporate loyalists who expected jobs for life—then discovered that they were viewed "as costs, not assets."

Trump: The Art of Survival by Donald J. Trump with Charles Leerhsen (Warner, \$5.99, August). Since the book's hardcover publication, someone had the sense to replace the original subtitle, *Surviving at the Top*, with one conveying a more desperate quality. And a chapter covering the past year has been added. But the subject isn't surviving. It's Donald Trump setting scores. Among those he bad-mouths are New York hotel queen Leon Helmsley, gossip columnist Liz Smith, and Frank Sinatra. It all makes for a kind of sleazy good read—so go ahead, indulge yourself.

Means of Ascent by Robert A. Caro (Vintage, \$15). From 1941 through 1944, writes Caro in the second volume of the projected four in *The Years of Lyndon Johnson*, LBJ invented a combat record, stole a primary, and grew rich peddling political services. Re-counting his 1948 Senate race against former Texas Governor Coke Stevenson, the book becomes a political thriller. Johnson violates every rule of decency. Caro sees the contest as a watershed. LBJ's media manipulation and unprecedented spending, he asserts, helped usher in the era of sound bites and superficial imagery, which have robbed politics of meaning.

What I Saw at the Revolution: A Political Life in the Reagan Era by Peggy Noonan (Ivy, \$5.95). Describing her years as a White House speechwriter, Noonan shows what a wonderful work-mith she is. Although a true believer, she seems to have kept her sense of humor among the power-mad and the obsequious who surrounded Reagan. Still, this funny book has a core of disappointment: Noonan ends up disillusioned.



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ch the President she revered. "The
ttle for the mind of Ronald Reagan,"
e writes, "was like the trench warfare
World War I; never have so many
ught so hard for such barren terrain."

Gorbachev: Heretic in the Kremlin by
asko Doder and Louise Branson (Pen-
in, \$9.95). Gorbachev, the authors re-
al, has less in common with Lenin
an with Jimmy Carter: He's a bright,
iggish hayseed from a southern farm-
g region—and always on a self-im-
ovement kick. The authors track Gor-
chev's rise and the growth of his inner
cle. Even with a new afterword, the
ok has been left behind by the swirl of
viet events, but it remains a useful,
inently readable primer on Gorba-
ev's roots, his rule, and the era of
asnost and *perestroika*.

**My Traitor's Heart: A South African
ile Returns to Face His Country, His
be, and His Conscience** by Rian Malan
intage, \$10.95). Though descended
om the architects of apartheid, Malan
ew up a South African liberal. Yet,
ough he socialized with and cared for
acks, he feared them. Faced with the
aft, which meant taking one side in
e struggle over apartheid, he left
me. In the mid-1980s, he returned.
urneying through backwater towns
nd white suburbs, he investigated a se-
es of nightmarish murders—of blacks
y whites, whites by blacks, and blacks
y blacks. His wrenching book depicts a
peless nation locked in hate and fear.

**Against Gravity: From Paris to Dakar
the World's Most Dangerous Race** by
d McCabe (Warner, \$15.95). At 47, leg-
ndary adman McCabe, of Scali McCabe
oves, suffering chronic ennui, quit his
b to compete in the treacherous Paris/
akar Rallye. *Against Gravity* de-
cribes the torturous endurance training
e and his girlfriend underwent and
eir game effort to finish the 8,000-mile
ce. McCabe's writing crackles with the
rill and terror of hurtling through the
ahara's bewildering emptiness.

A Year in Provence by Peter Mayle
intage, \$10). Maybe admen just get
at way. London exec Mayle dropped
at to live full-time in sun-drenched Pro-
vence. Life there revolves around the
ible, and the book offers a wonderful
astronomic tour. Life is also tougher
an you might expect: Mayle and his
ife struggle to restore an old farm-
ouse, fend off a plague of summer
uests, and survive the shockingly cold
inter. "Provence is full-blooded... and
can poleaxe people," Mayle warns. But
s this book (published simultaneously
ith a hardcover sequel, *Toujours Pro-
vence*) makes clear, he loves the place.

BY DENISE DEMONG

among edits the Books section.



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A SECOND OPINION ON THE DEMOCRATS' HEALTH PLAN

BY ROBERT KUTTNER



Their national health insurance bill reveals a strategy that is more than wrongheaded. It's futile

The Democrats' long-awaited national health insurance bill, sponsored by Senators Mitchell, Kennedy, Rockefeller, and Riegle, is an instructive disappointment. The Democratic leadership has calculated that universal health coverage is now a legislative possibility—but only by moving incrementally and not alienating any key interest group.

The Democrats' Health America bill builds on the present system of employer-provided health insurance by mandating that businesses provide coverage or pay a tax, the so-called play-or-pay approach. People without private insurance would get federal coverage. Costs would be restrained by an annual process of setting health budget goals, but those goals would not be binding.

The Democrats hope that as the legislative process unfolds, the present draft will be refined. However, it is rare for weak legislation to become progressively stronger; if anything, interest groups demand more concessions.

Our health system now has the worst of all worlds: a built-in bias toward escalating costs coupled with declining security for individuals and constraints on doctors' freedom to practice. As medical technology becomes more complex and expensive, doctors understandably seek to maximize their freedom to make clinical decisions and to purchase costly new equipment as they see fit. Hospitals seek to keep beds occupied, and they compete on the basis of the most up-to-date facilities and services. But insurance companies, which pay most of the bills, naturally seek to restrain costs or pass them along through higher premiums, deductibles, and patient co-payments. The federal government shifts costs to the part of the system that is privately insured.

TOTAL FAILURE. Insurance companies then respond by clamping down more tightly on the freedom of providers and by denying coverage to people or groups likely to get sick. Large employers, faced with premium costs escalating at about 20% per year, defend themselves by passing more of the costs along to employees. Small businesses defend themselves by providing no insurance at all.

The end result of this massive systemic failure is that 37 million people have no insurance—and that even the middle class is suddenly vulnerable to huge increases in premiums and out-of-pocket charges or to denial of insurance based on a "preexisting condition" if they change jobs. The system also leads to colossal administrative waste.

The cleanest solution is, of course, a "single payer" system, supported by tax revenues, in which everyone would be insured, nobody would be excluded because of a medical con-

dition, hospitals would have annual budgets and hence would not have to send bills, and doctors in private practice would bill the single-payer agency. This would not only provide security of coverage but it also would free doctors and hospitals from the endless paper chase. And it would provide greater autonomy for doctors to make decisions based on their best medical judgment rather than on the basis of what they could wring out of private insurers.

DUCKING THE ISSUE. A second-best solution would be the play-or-pay plan. But to achieve the gains of a single-payer system, a play-or-pay approach needs tight cost-containment features. Otherwise, play-or-pay simply extends many of the inefficiencies of the current system. Yet it is precisely this issue that the Democrats' plan ducks.

Interviews with key Democrats suggest that they concluded that doctors and hospitals would resist a single-payer system but might back a play-or-pay requirement as a new source of income. Doctors and hospitals, however, would resist cost-containment. Large businesses, which now bear exorbitant costs through employee premiums, would support shifting to a partly tax-supported system. And insurance companies, which would be put out of business by a single-payer system, could also be enlisted in the play-or-pay coalition but would resist tighter regulation. Finally, the Democrats concluded that a tax-supported single-payer system was fiscally improbable while play-or-pay had a less visible budget impact. Hence, the incremental approach and the absence of cost containment.

The bill's sponsors believe that once the system is in place, its logic would lead to direct regulation of cost. I hope they are right. But 20 years of experience suggests a patchwork system is just as likely to seek saving through coverage cuts, as well as a dumping of the sickest into the residual public system. Moreover, President Bush opposes the entire approach, and there is no veto-proof majority in Congress for the Democratic plan.

A different strategy would be to go for the best approach and make health a major issue for 1992. Eventually, doctors, hospitals, and businesses, might come around to the single payer approach. For the present system points towards more paperwork, more irrational constraints on doctors and hospitals, and, of course, higher costs. A few Democrats—such as Senators Paul D. Wellstone and Bob Kerrey—are already there. If ever there was a long-term political winner, it is this one. It's a shame to see the opposition party pulling it punches on its best issue.

ROBERT KUTTNER IS ECONOMICS CORRESPONDENT FOR THE NEW REPUBLIC AND AUTHOR OF THE END OF LAISSEZ-FAIRE

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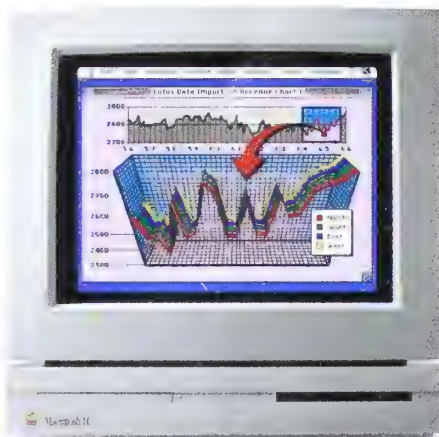
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Economic Trends

BY GENE KORETZ

THE MONEY SUPPLY: IT COULD RAIN ON THE RECOVERY'S PARADE

Heartened by signs of strengthening economic activity, many economists are suggesting that growth could surge rather sharply in the months ahead. Those who keep a weather eye on the U.S. money supply, however, are less optimistic. "The problem," says economist Lacy H. Hunt of the Hongkong-Bank group, "is that the pickup is occurring in an environment of extremely minimal monetary growth. Without more monetary fuel, the recovery is in danger of stalling out."

Hunt points out that the nominal money supply usually accelerates sharply as the economy shifts from recession into the early stages of a recovery. In the wake of the 1970, 1973-75, and 1981-82 contractions, for example, it hit double-digit rates on a year-to-year basis. In recent months, however, nominal M2 has slowed, and in May, it was not only be-

Group Inc. points out that M3 and M4, which add such items as large certificates of deposit, Treasury bills, and commercial paper to M2, have posted sharp declines recently. At the same time, the slowdown in the growth of credit demand from businesses and individuals shows no sign of reversing.

The Federal Reserve, ever concerned about inflation, appears to have ruled out further ease in the face of a strengthening economy. But economists such as Hunt and Lazar worry that the sluggishness of monetary growth, combined with pressure from regulators, can still choke off the incipient upturn. "You can't have a sustained recovery," warns Hunt, "unless a meaningful borrowing and lending cycle has the capability of getting under way."

HIDDEN STRENGTH IN HOUSEHOLD INCOME AND SAVINGS

With the personal savings rate down to a meager 3.6% in April and running close to its historical lows, many observers have argued that consumers simply do not have the capacity to expand spending very much in the months ahead. Economist William C. Melton of IDS Financial Services Inc. claims, however, that household spending power is greater than is appreciated because savings have been understated in an important sense.

The crux of the matter is the definition of income, since savings are simply the difference between the income (after taxes) received by people and their consumption expenditures. Melton points out that while the government counts employer contributions to pension and profit-sharing plans as part of labor income, along with pay, it doesn't count the benefits paid out of such plans. Rather than being regarded as current income, such payouts are treated like withdrawals from savings accounts.

None of this made much difference over most of the past 40 years, since employer contributions to benefit plans and benefit payouts tended to move on similar tracks. Starting in the mid-1980s, however, employer contributions stopped growing, while benefit payments took off. By 1989, the last year for which data are available, benefit payments were exceeding plan contributions by more than \$100 billion.

Melton's point is that such benefit payments are regarded as income by those receiving them. And if benefit payouts were substituted for employer contributions in calculating income, both

income and the savings rate would look a lot higher. For 1989, he estimates that such a change raises the personal savings rate by nearly three percentage points. "Considered from a cash-flow perspective," he says, "people have been saving more—and thus have more ability to accelerate spending—than the official savings rate suggests."

THE CRISIS OF HOPELESSNESS GROWS IN THE INNER CITY

The links among lack of education, crime, and joblessness in inner cities are getting tighter. Harvard University economist Richard Freeman told a recent Urban Institute conference that 20% of black men aged 16 to 34 were in jail or on parole or probation in 1989, and three-fourths of black prisoners 18 to 24 years old were high school dropouts.

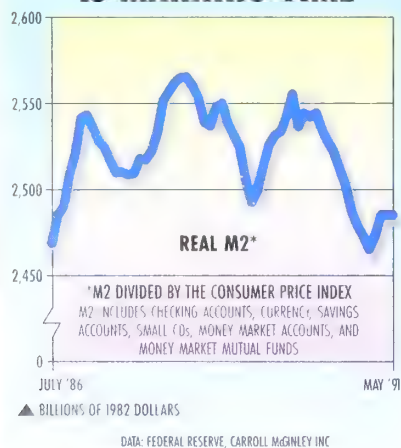
Poor employment prospects are clearly affecting the attitudes of disadvantaged youths toward crime. According to a 1989 National Bureau of Economic Research survey, some two-thirds of inner-city young men, black and white, now believe they can make more money from crime than from legitimate work. That's about double the percentage in a similar survey conducted 10 years earlier.

Although crime rates decline and desire for lawful employment rises with age, youthful criminals tend to become pariahs in the job market. Young men with records are consistently less likely to be employed in later years than those without criminal backgrounds, says Freeman, and when employed, they earn far less on an annual basis.

WHICH VIEW OF CAPITAL SPENDING DO YOU BELIEVE?

The Commerce Dept.'s latest capital-spending survey, conducted in April and May, estimates that real capital outlays rose at a 2.8% annual rate in the first quarter and will be up 3% in 1991 as a whole. Yet its gross national product report says real nonresidential fixed investment plunged at a 15.9% annual rate last quarter. Although divergences between the two measures are common, this one is unusually large. Because the GNP estimate is based on actual shipments data, economists at Donaldson, Lufkin & Jenrette Inc. think it is more reliable, particularly in times of uncertainty. Thus, they predict that "capital spending will fall, not rise, in 1991."

THE MONEY SUPPLY IS MARKING TIME



low the midpoint of the Fed's current target range but was just 3.2% above its level in May of last year—close to a record low in year-over-year growth.

Real, or inflation-adjusted, M2 tells a similar story (chart). This key component of the index of leading indicators was flat in April and May and has hardly grown in nearly five years. By contrast, it rose sharply in the late stages of the 1981-82 recession, and by early 1983, it had reached a new record high.

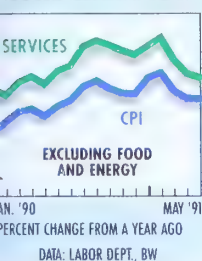
Other more inclusive measures of the money supply are also flashing disquieting signals. Economist Nancy Lazar of International Strategy & Investment

WHAT MIGHT DERAIL THE RECOVERY? INFLATION FEARS, FOR ONE THING

No pain, no gain: It's the inflation fighter's mantra. So far, however, the benefits of America's ninth recession since World War II don't look worth the cost. Despite some improvement in recent months, core inflation was no lower in May than it was when the recession began last July.

To be sure, past business-cycle behavior says that price growth will slow further. However, the improvement is shaping up to be disappointingly small, and looking further out, the economy seems headed back into that age-old battle between growth and inflation.

SERVICES PUSH DOWN CORE INFLATION



is the worry (page 48). The result is high long-term interest rates that threaten growth.

The bond market's fears are partly justified—but not for the months immediately ahead. Clearly, inflation improvement is not finished. After each of the past five recessions, price growth has declined during the first year of recovery. This time should be no different.

In the early stages of an upturn, business productivity improves as companies lift output faster than they put workers back on their payrolls, thus reducing the cost of making a widget. Also, businesses tend to hold the line on prices in order to regain their sales volume.

HIKES IN PRICES ARE FAIRLY TAME

Judging by the behavior of the consumer price index in May, the recession is beginning to have its typical cyclical impact on inflation. The CPI rose a modest 0.3% last month. Excluding food and energy, which eliminates the impact of the oil shock and temporary fluctuations in farm prices, the CPI increased only 0.2%. Measured over 12-month periods, this core rate of inflation has fallen to 1% after hitting 5.7% in February (chart).

Producer prices looked anything but tame in May. However, the month's 0.6% spike in prices of finished goods, including a 0.4% jump excluding food and energy, was caused primarily by onetime aberrations in prices for aircraft and tobacco. During the past year, finished-

goods prices are up only 3.4%, and the core rate has been slipping lower in recent months.

The improvement in consumer inflation has come mainly in services, where prices had been especially stubborn. Excluding energy, service inflation has dropped from 6.5% in February to 5.6% in May, led by slowdowns in rents, other homeowners' services, public transportation, personal care, and even a slight slowing in costs of medical care.

THE COST OF WIDGETS SHOULD STAY COOL

Don't expect any upward pressure on prices in the goods-producing sector in the coming months, either. Despite continued signs that manufacturing is firming up, there is still plenty of slack in production capacity and in factory labor markets to allow goods inflation to decline even in a full-fledged manufacturing recovery—although that's still not a sure thing.

Industrial production rose 0.5% in May, the second consecutive monthly gain. However, the advance was less than it appears. Utility output surged 3.9% last month, the result of unusually hot weather. Production in manufacturing alone rose only 0.2%.

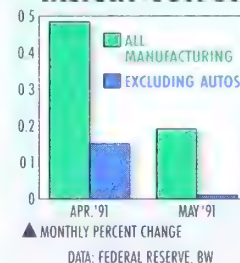
Moreover, the April and May gains in factory output were not very broad. An increase in auto production, from extremely low levels to still-low levels, accounted for almost all of the advance (chart).

Foreign trade continues to offer some support to U.S. producers. Exports increased by a sturdy 4.5% in April, to a record \$35.6 billion. Imports rose even more, however, widening the trade deficit to \$4.8 billion from \$4.1 billion in March.

The nascent recovery in housing has also provided some lift, but homebuilding is coming under the mercy of the bond market's inflation fears, which have pushed up long-term interest rates. The housing upturn stalled a bit in May as new starts held steady from April at an annual rate of 982,000. Starts are slightly below where they were in February.

Clearly, operating rates show plenty of room for production to rise without putting pressure on prices. The operating rate in manufacturing had ticked up in April, but it edged lower again in May, to 77.3%. Except for March's reading at 77.2%, capacity utilization was the lowest in more than eight years. Historically, operating

AUTOS ARE BOOSTING FACTORY OUTPUT



Business Outlook

rates have to rise to around 83% before generating worries about price pressures.

How fast manufacturing reaches that point will depend largely on the strength of the upturn in consumer spending. For now, retail sales are headed up. They rose a solid 1% in May, but continued gains at that pace in the face of weak income growth, low savings, heavy debt, and declining confidence just don't seem likely.

A bevy of onetime factors may be accounting for the seeming renewal of consumer spending, which has helped to lift production. In addition, some of the recent bounce in output might well be the result of extremely low levels of inventories. Stockpiles of goods at manufacturers, wholesalers, and retailers fell 0.5% in April, the third consecutive monthly drop (chart). Inventories were already low, the result of liquidation that had been under way since the recession began. Some amount of restocking may well be in progress, necessitating increases in output.

In fact, the need to replenish inventories in the face of rising demand is probably the best argument for a strong recovery. However, the economy may turn out to be a loser either way. If the rebound in consumer spending proves to be weak or temporary, the need to boost production will be short-lived. And if the recovery starts looking strong enough to fuel inflation, the bond market will push up interest rates and choke it down.

ECONOMIC GROWTH MAY BE STUNTED

But despite the relatively sanguine outlook for prices in the months ahead, the bond market's longer-term worries about inflation are partly justified. First of all, the recession's cyclical impact on price growth might turn out to be small and fleeting, particularly if the downturn's end is at hand. The recession has not been sufficiently long or deep to vent price pressures in any big way.

Even if the CPI continues to log subdued monthly

gains on the order of May's increase, inflation a year from now would fall to only around 4%, from today's 5% pace. If that turns out to be the starting point for the next inflation cycle, neither the bond market nor the Federal Reserve Board will be very pleased.

A SHARP LIQUIDATION OF INVENTORIES



down, and service prices will ease as well.

But after this near-term decline, further reduction in service inflation seems destined to be limited by the service sector's long-term failure to improve productivity. During the past decade, the growth in service productivity has been essentially zero. That limits productivity growth and inflation improvement in the overall economy as well.

Another problem is that the economy's long-term potential for growth appears to be edging lower. With the growth trends of productivity and the labor force apparently slipping to slightly above 1% each, the economy over the long haul cannot grow much more than 2% to 2½% per year without generating inflation.

All this adds up to a key point about the outlook. Neither the bond market nor the Fed wants a recovery that is strong enough to generate price pressures. In order to keep inflation under its heel, the Fed is not likely to allow growth to rise above its long-term potential for very long. So if the bond market doesn't put the clamps on the coming recovery, the Fed eventually will

THE WEEK AHEAD

DURABLE-GOODS ORDERS

Tuesday, June 25, 8:30 a.m.

New orders placed with durable-goods makers probably rose by about 1.9% in May, according to economists polled by MMS International, a division of McGraw-Hill Inc. The uptick would give strong evidence that the factory sector is climbing out of recession. The May gain is suggested by last month's increase in factory output, especially in the auto industry. Plus, the new-order index compiled by the National Association of Purchasing Management increased in May. In April, durable-goods orders advanced by a healthy 3%, but they fell in each of the three months before that. The expected gain in new orders indicates that

the backlog of unfilled orders also increased in May. Unfilled orders fell 0.5% in March and 0.8% in April.

PERSONAL INCOME

Thursday, June 27, 10 a.m.

Personal income likely increased by 0.5% in May after a small 0.1% gain in April, say the MMS economists. Increases in jobs and weekly pay indicate that wages and salaries grew last month. However, income growth has not kept pace with the increases in inflation and taxes over the past year. As a result, real disposable earnings are lower now than at the start of the recession. Consumer spending probably increased by a strong 0.7% in May. That's suggested by the 1% jump in retail sales. In April, consumer

buying edged down by 0.1%, led by weakness in new-car purchases.

LEADING INDICATORS

Friday, June 28, 8:30 a.m.

The MMS survey says that the government's composite index of leading indicators likely rose by 0.4% in May. Fewer new claims for jobless benefits, a longer factory workweek, and slower delivery times offset lower stock prices and a sharp fall in consumer expectations last month. Growth rates for real money supply and materials prices are estimated to have been flat. The expected increase would be the fourth monthly advance in the leading index—further proof that the recession is coming to an end. In April, the index rose by 0.6%.



UNDERSTANDABLY, THE IMPORTS ARE GETTING NERVOUS.

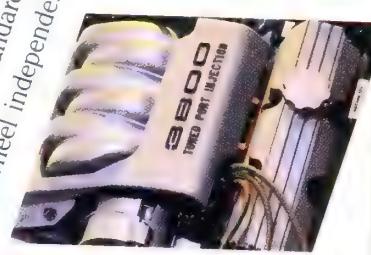
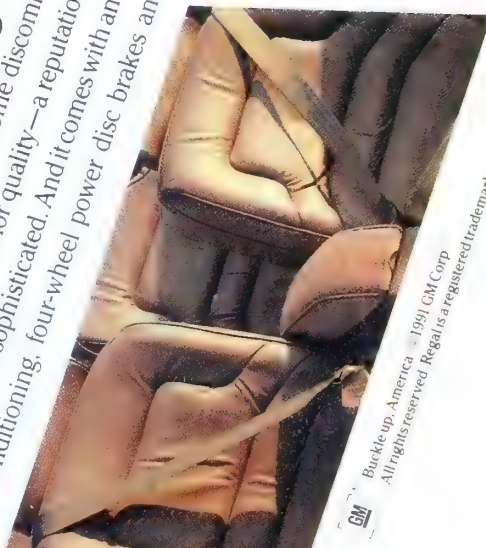
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THE BRAKES GO ON IN R&D

SPENDING CUTS COULD HARM U.S. COMPETITIVENESS

When George M. C. Fisher, chairman of Motorola Inc., mapped out research and development plans for 1990, he did what few executives dared: He raised R&D expenditures as a percentage of sales and profits and expanded the company's research horizons. Fisher is wary of what he calls U.S. industry's "rifle-shot" approach to R&D—focusing on small improvements in product development at the expense of riskier but potentially market-shaping research. "The more corporate R&D drifts toward the 'R,'" he says, "the less of a rifle shot it is." So again this year, Motorola is "moving more investment toward the 'R' side."

Fisher's fellow executives should take heed. A warning leaps from BUSINESS WEEK's annual survey of R&D spending: Corporate America, bedeviled by Japanese manufacturing wizardry and numbed by the recession, is squinting so hard at cost-cutting and tiny improvements in existing processes that it's in danger of missing the big picture. "The founding fathers have been succeeded by process-oriented managers," laments Donald N. Frey, professor of industrial engineering and management sciences at Northwestern University. He and others say this new generation of executives risks forsaking the pioneering research that led to such crucial discoveries as the transistor.

BUSINESS WEEK's survey, covering 910 public companies, won't calm Frey's fears. It shows that U.S. companies spent \$69.7 billion on R&D in 1990, up 7% from 1989 in today's dollars but just 2.2% adjusted for inflation. The 1990 results show the second-smallest real increase since the

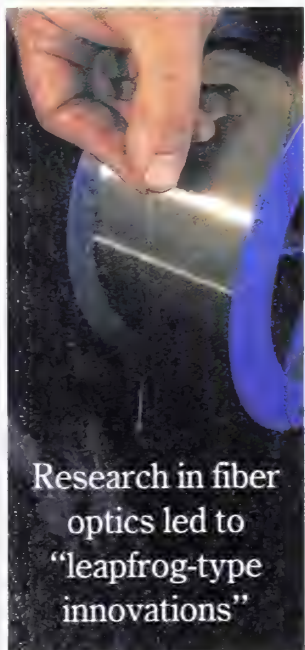
survey began (chart). And 1991 could be worse. In fact, the U.S. is in the greatest slowdown in R&D spending for real spending to match 1969 levels. "You can really see: The brakes have been applied," says John R. Gawalt, science resources analyst at the National Science Foundation's division of Science Resources Studies. The NSF projects no real growth in industry R&D spending in 1991.

BRUTAL DROP. It isn't all doom and gloom. After all, the recession is fading fast, and the slowdown is partly a result of diving profits. But the numbers nevertheless herald a turning point for R&D. In industry after industry, higher costs and stiffer competition are forcing cuts. And with no defense-led boom to drive up R&D spending, as happened in the late 1970s and early 1980s, these forces will keep real growth in R&D spending below 3% a year when things tick back up in 1994 or 1995, predicts Jules J. Duga, co-author of Battelle Memorial Research Institute's 1991 R&D forecast. The challenge for U.S. business is to compete on costs and development issues without harming research. Some companies say they're on the right track. But critics like Frey are dubious.

It is clear, however, that managers will have to spend more wisely—because few have money to burn. Telecommunications took the biggest hit in 1990. Led by a brutal 8% drop at American Telephone & Telegraph Co., which accounts for more than two-thirds of the industry's total R&D spending, telecom slipped 5% from 1989 in nominal terms. Aerospace, rocked by cuts in defense spend-



BELL LABS WAS ONCE THE PARAGON OF BASIC RESEARCH, BUT RECENTLY ITS REPUTATION AS A PIONEER HAS SUFFERED

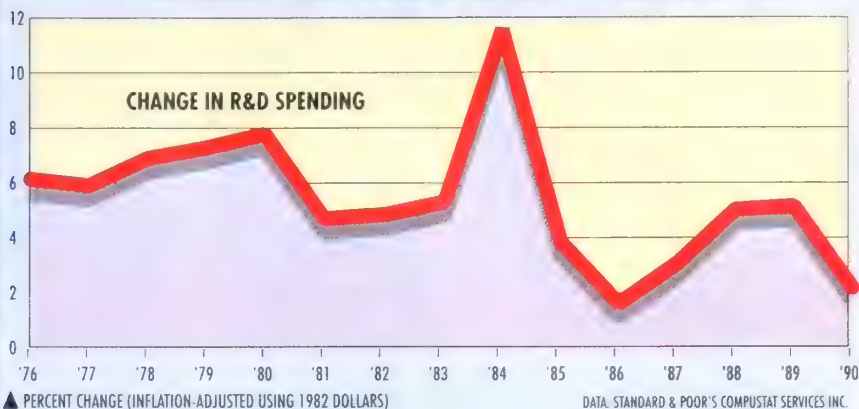


Research in fiber optics led to "leapfrog-type innovations"

ing, came in flat. The normally strong computer group weighed in with a lackluster 1% increase—led, if that's the word, by IBM's 6% decline. The automotive industry, with two of the country's top three spenders in General Motors Corp. and Ford Motor Co., was a mixed bag. Driven by the need to keep new models coming, Detroit managed a 5% increase despite ongoing losses in car and truck sales. But the carmakers' spurt was still two percentage points below that of the all-industry composite.



THE R&D SLOWDOWN: AN OVERVIEW...



...AND HOW 20 INDUSTRIES RANK

Industry	Percent change 1990 vs. 1989	R&D expenses Millions	1990 R&D as percent of sales	1990 R&D per employee
PUBLISHING & BROADCASTING	281%	\$12.9	3.0%	\$12,087
NONBANK FINANCIAL	24	88.8	0.7	2,617
HEALTH CARE	20	8,509.0	8.8	12,864
METALS & MINING	12	407.9	1.1	1,891
ELECTRICAL & ELECTRONICS	11	7,105.5	5.5	5,850
MANUFACTURING	11	3,132.4	2.9	3,780
CHEMICALS	10	5,160.2	3.9	9,177
CONSUMER PRODUCTS	10	1,821.3	1.4	2,037
SERVICE INDUSTRIES	10	106.3	0.8	810
FOOD	9	520.0	0.7	1,199
CONGLOMERATES	8	3,668.5	2.7	4,138
CONTAINERS & PACKAGING	8	93.8	0.9	953
FUEL	7	2,710.4	0.7	3,582
PAPER & FOREST PRODUCTS	7	391.8	1.1	2,022
OFFICE EQUIPMENT & SERVICES	5	15,849.6	7.9	11,751
AUTOMOTIVE	5	10,706.9	3.7	6,897
LEISURE TIME PRODUCTS	5	1,798.6	5.1	6,692
HOUSING	3	505.7	1.8	2,661
AEROSPACE	0	3,919.4	3.7	4,764
TELECOMMUNICATIONS	-5	3,162.1	3.6	4,825
ALL-INDUSTRY COMPOSITE 1990	7%	69,671.0	3.4%	\$5,936
ALL-INDUSTRY COMPOSITE 1989	10	65,231.0	3.4	5,523

DATA: STANDARD & POOR'S COMPUSTAT SERVICES INC.

Some businesses, of course, plow ahead. Health care, spurred by pharmaceutical and biotechnology companies that must develop new products or die, reported a 20% increase in R&D outlays, after gaining 13% the year before. Among the bigger players, Warner-Lambert Co. rose the most, up 23%. Biotech shot Amgen Inc. jumped 108%. Chipmakers also spent big, shelling out 14% more on R&D than in 1989. Intel Corp. slashed spending 42%. Motorola, the No. 1 U.S. semiconductor maker, which be-

cause of its diversity is placed in the broader electronics group, was up 24%.

Such bright stars are the exception, though, and most U.S. companies seem to be losing ground to overseas rivals. New figures from the Organization for Economic Cooperation & Development in Paris show that on an inflation- and currency-adjusted basis, U.S. corporate R&D spending actually fell 1.6% in 1990. Other nations tallied so far all posted gains: France, 7.5%, Italy, 3.3%, Canada, 2.9%, and Germany, 2.8%.

It's not that companies don't see the perils ahead. "They don't just lightly wipe out research—they know there's a cloud over their heads already," says Peter Likins, president of Lehigh University and a member of the Council on Competitiveness, a Washington-based alliance of business, academe, and labor. "But hell, this is a recession, and you gotta cut money somewhere."

Under intense economic pressure, companies are struggling to get more bang for their buck. The current fashion

Top of the News

in cost-saving research involves alliances among competitors. Since 1988, Detroit carmakers have set up five consortiums researching everything from electric-car batteries to reformulated gas. And in June came the disclosure that IBM might provide ultrafast chips to Apple Computer Inc. in return for software development help.

More often, though, companies simply give risky projects the ax. Lockheed Corp. plans to focus less on weapons research and more on technologies—such as improved computer-aided de-

The drive to rein in costs and boost product development isn't all bad. For one thing, says Lockheed's Caren, "it will force more careful planning." True enough. But all too often, companies are going too far, warns Joseph G. Morone, associate director of the Center for Science and Technology Policy at Rensselaer Polytechnic Institute.

Morone is studying how companies manage technology. He finds that most overemphasize so-called incremental innovation—operational fine-tuning. By contrast, the outfits that manage tech-

And Motorola has adapted state-of-the-art manufacturing management to basic research by setting firmer standards for reliability and acceptable failure rates. "Even when you're working on breakthrough products, there's a lot of waste that can be cut," says Fisher.

FEELING HEAT. AT&T's Bell Laboratories typifies the struggle between basic and applied science, or between research and development. Bell Labs was once the paragon of basic research, with several Nobel laureates to its credit, but its pioneering reputation has waned as it fo-

RESEARCH AND DEVELOPMENT: THE BIGGEST SPENDERS

Company	1990 R&D expenses Millions of dollars
GENERAL MOTORS	\$5,342
IBM	4,914
FORD	3,558
AT&T	2,433
DIGITAL EQUIPMENT	1,614
GENERAL ELECTRIC	1,479
DU PONT	1,428
HEWLETT-PACKARD	1,367
EASTMAN KODAK	1,329
DOW CHEMICAL	1,136

THE TOP 10 R&D SPENDERS PER EMPLOYEE

Among all companies	1990 R&D expenses per employee
GENENTECH	\$81,316
GENETICS INSTITUTE	78,547
CHIPS & TECHNOLOGIES	68,456
WEITEK	58,986
AMGEN	58,290
TELEMATICS INTERNATIONAL	54,604
BMC SOFTWARE	54,127
ALZA	51,111
CENTOCOR	50,987
MIPS COMPUTER SYSTEMS	44,552

DATA: STANDARD & POOR'S COMPUSTAT SERVICES INC.

THE TOP 10 R&D SPENDERS PER DOLLAR OF SALES

Among all companies	1990 R&D expenses as percent of sales
GENETICS INSTITUTE	112.4%
CENTOCOR	71.0
CHIRON	40.7
GENENTECH	36.0
ALZA	35.2
TELEMATICS INTERNATIONAL	31.0
CONTINUUM	28.1
HOGAN SYSTEMS	26.2
BMC SOFTWARE	24.7
CYPRESS SEMICONDUCTOR	24.7

sign—that help lower costs. "That means some program R&D efforts will go by the wayside," says Robert P. Caren, vice-president of science and technology. What's true for Lockheed is true for aerospace as a whole: A new NSF survey notes that the industry is planning a 1.7% cut in domestic R&D expenditures in 1991—making it the only sector expecting a decrease in nominal-dollar terms.

HEFTY HIKES. Cost-squeezing extends even to areas where R&D spending rolls along. More expensive equipment and more insidious diseases have driven the average cost of developing a new drug at big pharmaceutical companies to \$231 million, more than double the inflation-adjusted cost a decade ago, reports a 1990 Tufts University study. Even hefty hikes in budgets can't keep up. Some companies, such as Merck & Co. and Bristol-Myers Squibb Co., have countered by leaving much of the pioneering research to startups, says health care analyst Viren Mehta, of Mehta & Isaly in New York. The big boys then license the technologies, putting their R&D dollars more into development—which they back up with a strong marketing push. "It's the brave new world of M&D companies, rather than R&D," Mehta says.

nology exceptionally well aren't afraid of risk. "What you find is that companies like Motorola, Corning, and GE Medical built their leadership positions in highly competitive global markets through ambitious, radical, leapfrog-type innovations—cellular phones, fiber optics, and medical imaging," says Morone. "In each case, developing the product was a long, painful process—and the companies had to swallow major losses along the way."

Some companies seem well aware of what Morone calls the imperative to balance incremental improvements with fundamental research. Microsoft Corp. in May revealed plans to build a lab dedicated to basic research in software—looking, for example, at ways to make computers understand everyday language rather than arcane commands.

**'Even when you're
working on breakthrough
products, there's
a lot of waste'**

causes more on developmental problems.

AT&T insists that the 'R' part of its R&D budget hasn't suffered. But any time total R&D funds ebb, research can feel the heat. To help ease that pressure Bell Labs is trying to use its research more effectively—in part by setting up programs to increase communication with the development side so that new breakthroughs won't flounder. "You carry through the technology transfer more into the development side, as opposed to kind of throwing it over the wall and letting them work with it as the might," says Birute K. Vitenas, Bell Labs' chief financial officer.

All these efforts to strike a better balance between the often-competing arm of research and development are noble experiments. But breakthroughs take time. Then companies must develop their innovations for the marketplace. So how well U.S. companies are managing R&D today won't be apparent for years—until the next generation of revolutionary products does, or does not, appear. The problem is, by then it could be too late.

By Robert Buder in New York, with John Carey in Washington, Joseph Weber in Philadelphia, Eric Schine in Los Angeles, and bureau reports



ROLLED UP AND NOWHERE TO GO: MINIMILLS ARE BITING INTO SALES

WHY STEEL IS STILL BENT OUT OF SHAPE

Large producers were supposed to have bounced back by now, but . . .

Whatever happened to the great steel recovery? After a decade of tuning up mills with \$14 billion of the latest technology, America's big steel producers were itching to test their mettle in a recession. They figured they were lean enough to make profit in all but the worst of slumps. Guess again, folks. Instead of weathering this recession, the steel industry is being battered by it. In the quarter ending June 30, the big six producers—Armco, Bethlehem, Inland, LTV, National, and USX—may lose \$28 on each \$430 ton of steel they ship, down from a \$16-per-ton profit in last year's first quarter. For all of 1991, says John E. Jacobson of US Consultants in Philadelphia, steel shipments may slump 11%, to 76 million tons, and the companies could lose as much as \$1.3 billion. "You'd expect we'd be in better shape" after all the restructuring the industry has done, laments Bethlehem CEO Walter F. Williams.

TREMENDOUS PROGRESS. To be sure, the steel industry is stronger than in the mid-1980s, when large producers, including LTV Corp. and Wheeling-Pittsburgh Steel Corp., filed for bankruptcy. But that's half the trouble. Big Steel is now being hurt mainly by domestic minimills that recycle scrap steel and by "reconstituted" mills that were spun off into ESOPs or restructured through

bankruptcy proceedings. These small producers are biting into sales just as Big Steel is reeling from weak demand in autos, construction, and other key markets. Large steelmakers "have made tremendous progress," notes Charles A. Bradford, an analyst at UBS Securities Inc. "But so has everyone else."

The situation is about to get even dicier. The Bush Administration vows not to renew so-called voluntary-restraint agreements that have held steel imports to 20% or less of the U.S. market since 1984 and are due to expire next March. Domestic producers warn that this will lead to foreign dumping. But the Administration believes that, despite its problems, U.S. steel is now strong enough to hold off imports. At a price. Foreign ownership, now about 19%, is almost sure to increase as big American producers scramble for capital. And restructuring is likely to continue well into the 1990s.

It wasn't supposed to happen this way. In the 1980s, U.S. steel companies poured an

average of \$2.5 billion annually, or 8.5% of sales, into capital spending—with the majors making 60% of the investment. They also slashed employment by 58%, to 164,000, and cut capacity by 30%. Productivity zoomed: It now takes U.S. makers just 5.3 man-hours to produce a metric ton of cold-rolled steel. That's 44% fewer than 10 years ago and bests Japan's 5.6 and Germany's 5.7.

STRATEGY CHINKS. Meanwhile, big U.S. producers have greatly improved quality while focusing more on high-end sheet steel. Formed into car fenders and appliances, sheet steel now represents nearly all of National and LTV's sales. In theory, it commands higher margins than the commodity steel now dominated by minimills and other smaller companies.

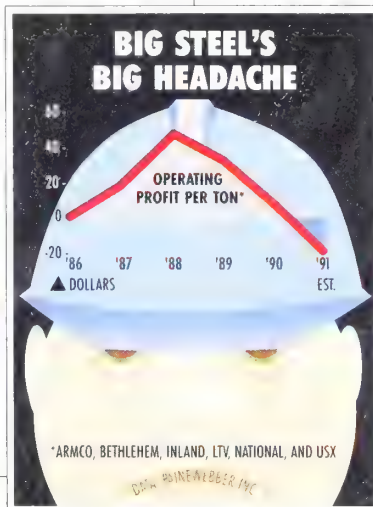
This recession, however, is showing the chinks in Big Steel's strategy. For one thing, U.S. companies were too far behind to catch up so soon. Even now, only two-thirds of U.S. raw-steel processing uses efficient continuous casting. That's up from 29% in 1982, but it's still behind Germany's 89% and Japan's 93%. To really pull even in process technology, says Bethlehem's Williams, U.S. companies would have had to do twice as much capital spending in the '80s.

Meanwhile, the investments steelmakers made have so far mainly benefited their customers. In the early 1980s, says P. T. Sullivan, executive director of purchasing for Ford Motor Co., up to 20% of Ford's steel was delivered late, and 8% was rejected because of poor quality. Now, he says, late deliveries and rejections are under 1%—comparable with Japanese and German levels.

But in the rush to please big customers, steelmakers have often overbuilt. For instance, the current glut of capacity for galvanizing, which improves rust resistance, could reach 4 million tons by 1994, estimates Tony R. Taccone, a Beddows & Co. consultant in Pittsburgh. And key customers, such as the auto makers, General Electric, and Whirlpool, have the muscle to demand rock-bottom prices. On average, gripes LTV Chairman

David H. Hoag, steel fetches the same price as it did in 1984.

A major reason for this is that restructuring has cracked Big Steel's oligopoly. Reconstituted mills now ship 28% of U.S. steel, estimates Paine-Webber Inc. analyst Peter F. Marcus, and the huge labor concessions that many of these companies won often give them a cost advantage. And minimills have jumped to



6% of the market, from 2% in 1979. They've also surprised the big companies by moving up into traditional strongholds such as structural steel and even low-end sheet steel. Most of these gains have come at the expense of the majors: In 1979, the eight biggest steel companies controlled 78% of the U.S. market; today's big six have about half.

The question now is whether removing voluntary restraints will hurt domestic producers. Since 1990's first quarter, imported steel's share of the U.S. market has jumped four points, to 19.5%, says the American Iron & Steel Institute. Domestic makers warn that without protection, imports may soar, as they did in the early '80s, when they

reached 30% of shipments. But, barring a big rise in the dollar, many experts think that's unlikely. Marcus predicts that importers will lose share in the '90s.

LARGER CHUNKS. Japanese and European makers seem more interested in buying into U.S. production than importing. NKK Corp. now owns 70% of National Steel. In May, Kawasaki Steel Corp. increased its share of Armco's flat-rolled-steel division from 45% to 50%. LTV is discussing selling steel operations to Japan's Sumitomo Metal Industries Ltd. and France's Usinor Sacilor, while Bethlehem is negotiating a venture with British Steel Corp. Even USX has said it would sell its steel operations for the right price. All told, foreign companies,

mainly Japanese, invested some \$4 billion in the U.S. steel industry during the '80s, most of it in about 30 joint ventures with U.S. producers.

Despite all the help, Big Steel is still far from its goal: to be profitable running at as little as 60% of capacity. Kenneth Iverson, CEO of Nucor Corp. says the industry is "two or three years away from that"—and that may be optimistic. In this recession, red ink started flowing in 1991's first quarter, with operating rates still at 73%. More buyout and plant shutterings may finally get the domestic steel industry to its goal. By then, it's likely to be smaller—with a lot more of it under foreign control.

By Michael Schroeder in Pittsburgh

COMPUTERS

'MINI' SOLUTION, MAXI RISK FOR WANG

The IBM deal adds cash. Customers are another story

It bore all the markings of a desperate move. On June 18, at a hastily called New York news conference, Wang Laboratories Inc. announced it would sell computers made by IBM—and help customers replace its own minis with those of its archrival.

The deal should get Wang as much as \$100 million in much-needed revenues over the next 2½ years. But Wang loses something, too. Chief Executive Officer Rick W. Miller is handing his minicomputer business to IBM on a platter. He intends to resell Big Blue's RS/6000 reduced instruction-set computers and PS/2 personal computers, giving them added value by loading them with Wang imaging software. In addition, Wang plans to sell IBM's AS/400 minis to those customers who bought the 60,000 Wang minis installed since 1977. Now, Wang can exit the money-losing mini business—and IBM will pick up the pieces.

SEEING RED. Wang is just the latest computer manufacturer to turn to a competitor for help. In fact, Miller's Apr. 17 flight to IBM's Armonk (N.Y.) headquarters was followed eight weeks later by a team from Apple Computer Inc. But Miller's motivation is different, and more urgent: To halt Wang's wrenching downturn, he must quickly rebuild the company's revenues with imaging software, which converts paper documents into electronic pictures, and office software—word processing, electronic mail, and the like.

It may be the Lowell (Mass.) company's best hope of averting slow dissolu-

tion. When he joined Wang in August, 1989, Miller predicted a return to profits by this year. Rapid asset sales and deep expense cuts failed to turn the tide. After a first-quarter, \$12.6 million operating profit last September, the weak economy drove Wang back into the red. Now, analysts predict that Wang's June 30 fiscal year will end with its third consecutive annual operating loss, clocking in at \$142 million, compared with a \$513 million operating loss last year.

Another reorganization, the company's second in two years, is ahead. A new round of layoffs should slash 5,000 to 7,000 employees from its 17,000-person work force, say insiders. And now that Wang is reselling IBM's PS/2, it's not at all certain that the company should continue designing and manufacturing its own PCs, an estimated \$400 million-a-year business. Wang employees say Miller will soon break the company into three separate businesses: one concentrating on its new office and imaging software, another focusing on existing mini customers, and a third for consulting and service.

By cutting a deal with IBM, Miller is,

in effect, executing the most sorely needed phase of the breakup. Wang's equipment sales have been in free-fall, slipping more than 20% a quarter for the

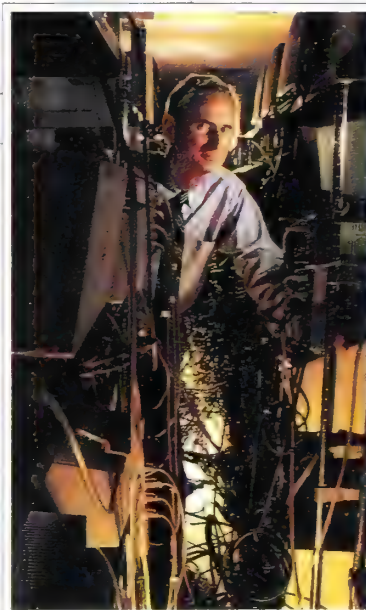
last two periods. Analysts expect total revenues for the year ending June 30 to drop to \$2.1 billion, from \$2.6 billion last year. Selling IBM's machines says Miller, "give customers a clearer understanding of our direction and far less risk for staying with us in the future."

WHAT GIVES? It's the deal that Miller may live to regret. In opting to sell IBM computers in place of its own minis, Wang is betting that it can successfully sell software to run on the equipment made by its fiercest rival. And the IBM deal puts Wang's \$900 million in annual service

revenues up for grabs as well. Wang says it will service the equipment it sells. But if it steers customers to IBM computers, asks PaineWebber Inc. analyst Stephen K. Smith, why shouldn't they buy IBM service? Wang has "given away the farm," he says.

The deal puzzles even some longtime Wang customers. "I don't know that we would be a significant purchaser of IBM hardware from Wang," says Helen Van Eeden, a senior vice-president at Shearson Lehman Brothers and the chairperson of an advisory council representing Wang's 30 largest customers. By giving customers a Big Blue security blanket, Miller has paid a high price for survival.

By Gary McWilliams in Boston



SHORT CIRCUIT: CEO MILLER FACES A THIRD STRAIGHT YEAR OF LOSSES

S PETE WILSON TRYING TO MUTE A SHAREHOLDER ACTIVIST?

California's governor is getting stung in his bid to control CalPERS

It started as a money grab: Desperate to close California's projected \$14.3 billion budget gap by July 1, Republican Governor Pete Wilson eyed surplus funds in the \$63 billion California Public Employees' Retirement System. Tinkering with formulas and assumptions could provide as much as \$2.5 billion. Then came the power grab: In his budget package, Wilson also proposed reconstituting CalPERS' board, dismissing representatives of retirees, and stacking it with members that he and state legislators would point.

What's Wilson up to? It's not clear, but his plan has incited a don't-know. Unions have threatened a boycott of California companies, CalPERS' supporters are arguing the Business Roundtable with underfunding, and a slew of interested parties are crying foul. State Treasurer Kathleen Brown, a Democrat who would replace her ex officio board seat, says the move is reminiscent of court-packing days.

NEXUS. Chalk up much of the fuss to CalPERS' position on the cutting edge of shareholder activism, particularly on such corporate governance issues as boards, shareholder advisory committees, and antitakeover defenses. The fund's backers charge that Wilson wants to score points with big business. One story has Wilson promising executives that a new board would curtail CalPERS' meddling. The proposal has lobbied to some legislators as a "get CalPERS measure," according to several people. One such report came from CalPERS' Chief Executive Dale M. Hanson, who read about the board revamp in the June 14 *Sacramento Bee*. Since tampering with CalPERS would slow the shareholder movement, some activists saw the tracks at the Roundtable, which is often portrayed as CalPERS' archenemy, or of Roundtable members.

Denials flew as soon as the fight broke out in public. "There was absolutely no nexus between the board's so-

called corporate-governance role and the changes that we are proposing in the board's makeup," says David J. Tirapelle, director of Personnel Administration and one of the governor's representatives on CalPERS' board. Perhaps, but Hanson's supporters note that Wilson asked for little from the \$35 billion California State Teachers Retirement System, 75% of whose board the governor

it won a say in director nominations. CalPERS funds have supported several members of the "shareholder industry," including consultants Institutional Shareholder Services, Analysis Group, and Providence Capital.

As the largest pension fund, CalPERS contributes 16% of the budget of the Council of Institutional Investors (CII), the Washington-based group of activist funds. And CalPERS paid consultant Graef S. Crystal for an executive compensation study that lays groundwork for CII's activities in that field. Defanging CalPERS would deal a psychological blow, too. Says Sarah Teslik, CII's executive director: "Whenever we need a fund to do something first, they're always the first to volunteer. Without CalPERS, a lot of funds wouldn't come forward."

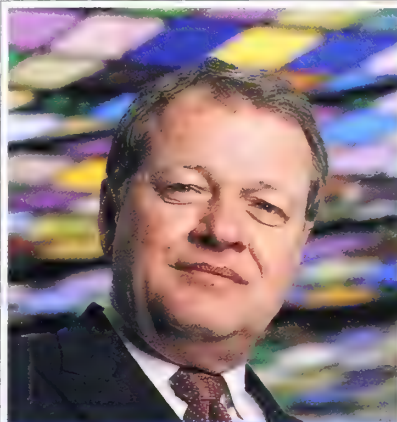
COMPROMISE? Wilson may have hoped he could slip through the board changes by offering state legislators a way to close the budget deficit while reducing the need to raise taxes. Or he may have figured that he couldn't get CalPERS' money now, or control of its future surpluses, without a board restructuring.

But Hanson has risen to the challenge. To head off the makeover, CalPERS offered on June 17 to hand over \$1.6 billion in two funds now used to cover cost-of-living adjustments for current retirees, provided that the state allows CalPERS to make up part of the payments

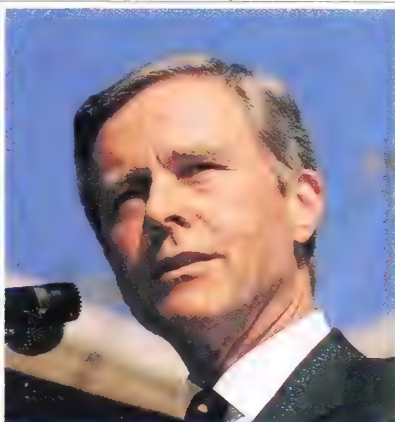
in another way. In return, Wilson would agree not to tamper with the board and not to boost the fund's return target from 8.5% to 9.5%, which would free another \$700 million in funds, until Hanson's review of the matter is completed.

Now, Wilson is on the spot. With much of what he wants on the money side, he must decide whether to continue his fight to control the board. California's Democrat-controlled Senate is likely to go along, reluctantly, with whatever he does, just to get a budget deal. But Assembly Democrats, who want no part of clawing back pension-fund money or throwing union members off the board, could yet put up a roadblock. In the days ahead, other states trying to balance their budgets will be watching. But perhaps not nearly as closely as corporate executives and institutional investors.

By Judith H. Dobrynski in New York, with Ronald Grover and Eric Schine in Los Angeles



CEO Hanson heard about Wilson's plan to 'get CalPERS' from legislators



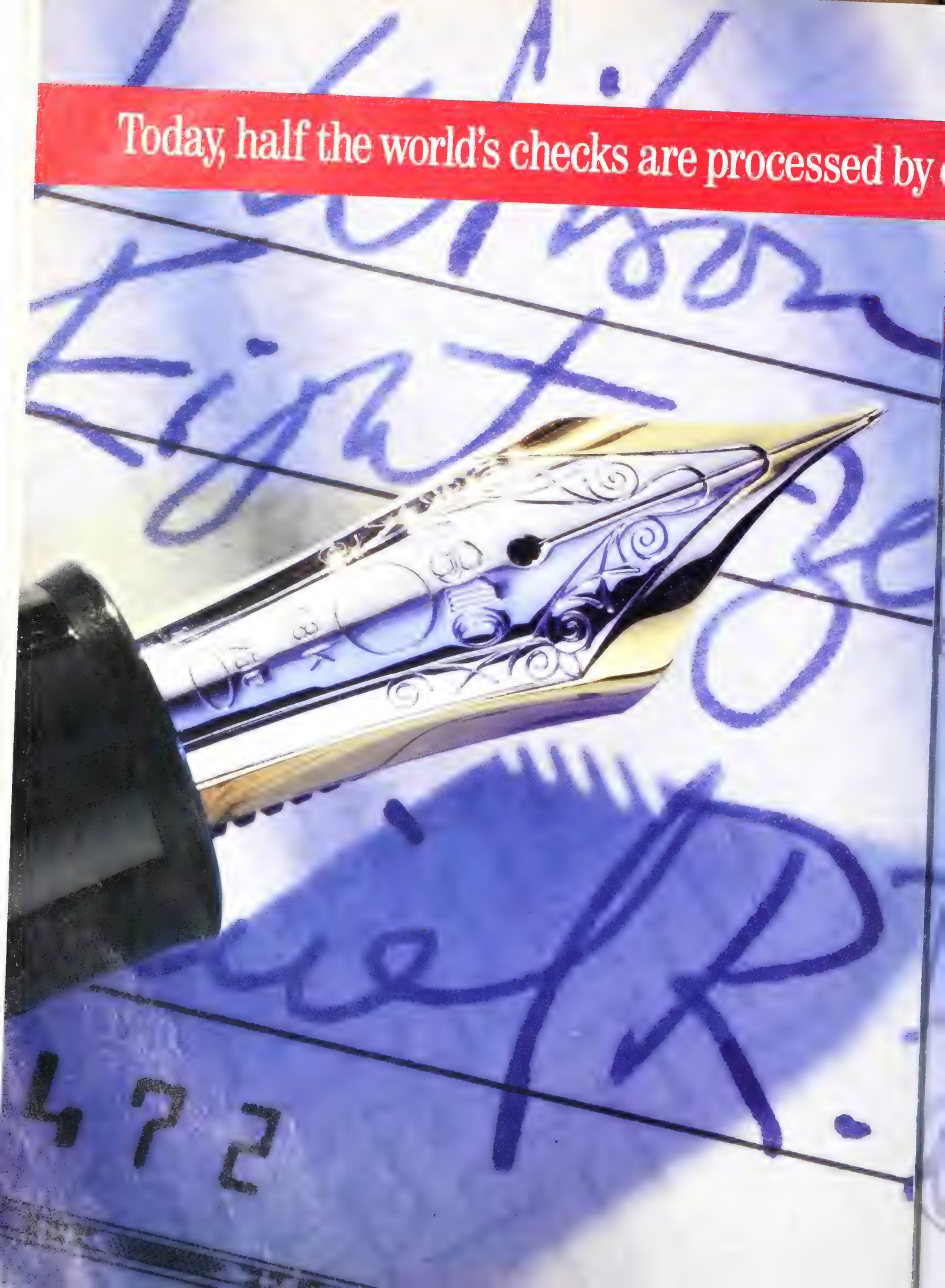
Wilson wants the right to appoint a majority on the board

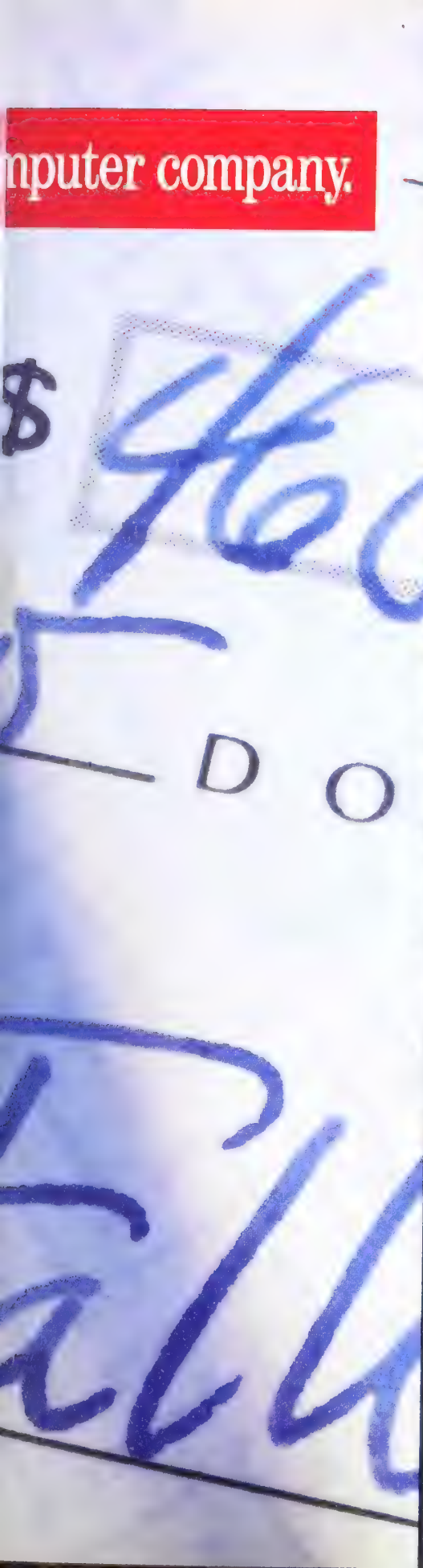
does appoint and whose voice on corporate governance is meek.

Meanwhile, H. Brewster Atwater Jr., CEO of General Mills Inc. and chairman of the Roundtable's task force on corporate governance, maintains that there wasn't "a shred of truth" to the notion of its involvement: "We've never had any discussion about this with anyone or among ourselves." Atwater, who dashed off a denial letter to Hanson, adds that the Roundtable would not favor a board of political appointees.

Roundtable members—and most corporate chieftains—would hardly oppose stifling CalPERS, though. Besides sponsoring about a dozen shareholder resolutions each proxy season, CalPERS has taken on management at General Motors Corp. over CEO selection and board composition and at ITT Corp. over CEO Rand V. Araskog's pay. It backed dissidents at Sears, Roebuck & Co. this year and at Lockheed Corp. last year, where

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We make it happen

Commentary/by Bill Javetski

HOW BUSH COULD HELP MOSCOW'S ODD COUPLE GET ALONG

What a difference a *da* makes. The last time Soviet political maverick Boris N. Yeltsin toured Washington, he got a cold shoulder at the White House and was treated like just another political wannabe on Capitol Hill. But after getting a yes vote from his constituents and winning the first popular election in Russian history, the President of the Russian Republic arrived in Washington on June 18 to find the red carpet all rolled out for him.

The Administration arranged meetings with Defense Secretary Richard B. Cheney, Commerce Secretary Robert A. Mosbacher, Vice-President Dan Quayle, and President Bush himself. Congress stopped short of inviting him to address a joint session but asked Yeltsin to confer with the bipartisan leadership of both houses and chat with both foreign-affairs committees.

DILEMMA CITY. Yeltsin's presence in Washington raises a thorny question for Bush: Is it possible to embrace this fiery populist, who calls for the rapid dismantling of the state-controlled economy, without undermining Soviet President Mikhail Gorbachev, who heads the central government?

Proud of his foreign-policy prowess, Bush thinks he's up to the task of dealing with two powerful leaders in Moscow. But caution is in order. Bush has to be careful not to fall into traps set by such leading conservatives as Senators Jesse Helms (R-N.C.) and Orrin G. Hatch (R-Utah), who are eager to push Gorbachev off center stage. They prefer the anticommunist Yeltsin as an alternative to Gorbachev—and they're using his visit to intensify a campaign to shift U.S. attention from the central Soviet government to the republics. Senate Minority Leader Bob Dole (R-Kans.), for example, wasted no time in telling Yeltsin that he favors direct trade in agriculture between the U.S. and the Russian Republic.

As Bush well knows, too-rapid devolution of power to the republics could reduce the Soviet Union, with its huge

arsenal of nuclear weapons, to anarchy. Even in Gorbachev's embattled state, he continues to deliver on key U.S. objectives, ranging from the fall of the Berlin Wall to an impending strategic-arms deal.

But Bush has his own good reasons to squeeze into Yeltsin's photo op. The President's strong backing of Gorbachev backfired earlier this year when Soviet troops staged a crackdown in the Baltics. It's dangerous for Bush to put all his eggs in Gorbachev's basket. With Soviet politics so fluid, Bush risks leaving the U.S. ill-prepared to establish contacts with possible Gorbachev

move by two master politicians. The bottom line is that Gorbachev and Yeltsin need each other. Under fire from conservatives back home, Gorbachev needs Yeltsin's popular support to lend legitimacy to any steps toward reform. And Yeltsin, despite his electoral victory, has no control over key institutions, such as the military, the Communist Party, and the KGB, which still back Gorbachev. Bush's challenge is to keep the momentum for reform alive by pressing both leaders to work together in nurturing free-market economics and the democratic process.

While Gorbachev's credentials are proven, Yeltsin is more of a wild card. He has yet to deliver on any of his rhetorical promises. The trick for Bush is to hold Yeltsin to them—from privatizing industry to signing a new union treaty—and not let him use his new clout to undermine Gorbachev. "It's not clear that Yeltsin can carry out reform in Moscow by himself, much less get people in Vladivostok to do what he wants," says Arthur A. Hartman, a former U.S. ambassador to the Soviet



successors as they emerge in Moscow and the republics.

The President doesn't have to make an either-or choice between Gorbachev and Yeltsin. It's in U.S. interests to cultivate solid relations with both men. In April, the two Moscow rivals saw fit to become allies—at least on paper. They, along with the leaders of eight other republics, pledged to work cooperatively to devise a new constitution that would share power between the central authorities and the republics and provide a base for moving to a free-market, democratic system.

This alliance is more than a tactical

The ideal Soviet leader is probably a person with Gorbachev's power base and Yeltsin's popular appeal

Union.

Bush has clout: He calls the tune on Western aid. That not only affects Gorbachev but also affects Yeltsin. At the top of Yeltsin's wish list is securing private investment and aid for the Russian Republic. Bush should insist that any aid flow through the central government to the republics and be conditional on Yeltsin and Gorbachev maintaining their partnership. Bush has leverage over Gorbachev, too. Any aid should be closely tied to the democratic and economic reforms that Yeltsin represents.

The ideal leader for the Soviet Union is probably a composite of Gorbachev and Yeltsin, a person with Gorbachev's power base and Yeltsin's popular appeal. But George Bush doesn't have the ability to force that kind of leader to emerge. The best he can do is use his leverage to keep the two Russian leaders moving toward each other—or run the risk of a dangerous breakup of the Soviet Union.

WASHINGTON HAS HOMEBUILDERS PITTING NAILS

They say new FHA mortgage rules push many buyers out of the market

After 3½ months of marriage, Kim and Gary Topper of Sandy Springs, Ga., want to "quit renting and get ourselves some equity," Gary says. The couple, both 24, spend weekends poking through closets and checking out floor plans of model homes. With help from Kim's parents, "we've got at least enough for a 5% downpayment" on a \$120,000 home, says Gary, a security systems salesman.

But new Federal Housing Administration rules, which require home buyers to come up with more up-front cash as of July 1, could force the Toppers to increase their downpayment by \$1,000. "Boy," says Gary, "that would make it tough for us to buy."

The fear that thousands of borrowers could be forced out of the market has the nation's homebuilders up in arms. Industry groups complain that the changes, which hit just as housing is beginning to snap back from a three-year slump, couldn't have come at a worse time. "You'd expect the Administration to come up with an anti-cession policy—not steer people away from home buying," says Warren Lasko, executive vice-president of the Mortgage Bankers Association of America.

TALKING AWAY. Like many government regulations, the FHA requirements started with the best of intentions. A 1990 Price Waterhouse & Co. study found that the FHA's main insurance fund, which guarantees low-downpayment mortgages for middle-income buyers, was losing \$200 million a year. The reason: borrowers could buy a home with a downpayment of less than 5% and could finance most closing costs. On a \$100,000 house, a buyer might borrow \$98,350—and then roll in the 3.8% FHA insurance premium as well. With so little of their own money at stake, they might walk away from the home if its value fell. The FHA's default rate hit 16% in the late '80s before falling to 11% last year.

The answer was higher insurance premiums, stricter solvency rules, and bigger equity requirements. After five months of wrangling over how hard to



GARY AND KIM TOPPER HOUSE-HUNTING IN ATLANTA

FHA LOANS GET PRICIER

The Housing & Urban Development Dept. is tightening up on mortgages insured by the Federal Housing Administration. But the Mortgage Bankers Assn. says HUD went too far. The effect when buying a \$100,000 home:

	Old law	1990 law	
		MBA estimates	HUD regulations
AMOUNT THAT CAN BE FINANCED	\$98,350	\$97,750	\$97,124
REQUIRED DOWNPAYMENT	4,650	5,250	5,876
ADDITIONAL COSTS	1,500	1,580	1,580
CASH NEEDED	6,150	6,830	7,456
CHANGE FROM OLD LAW		\$680	\$1,306

DATA: MORTGAGE BANKERS ASSN

hit home buyers, Congress and the Housing & Urban Development Dept. agreed to limit FHA financing for the house and closing costs to 97.75% of the property's value (98.75% for houses worth \$50,000 or less).

But a funny thing happened when the language of the 1990 National Affordable Housing Act was translated into

regulations. The FHA made the rule stricter: only 57% of closing costs could be financed. On a \$100,000 home with typical closing costs, the rule requires a total of \$7,456—\$1,306 more than under the old rules, and \$626 more than the language of the law requires (chart). "We swallowed the idea that buyers had to come up with more cash—but HUD doubled the hit," gripes Representative Bruce F. Vento (D-Minn.), a key negotiator on the housing bill. "They broke the deal we made."

OVERSTATEMENT? Not so, says HUD. Negotiations over the law "were always based on capping closing costs," not on limiting loan-to-value ratios, says HUD Assistant Secretary John C. Weicher. Even without the 1990 law, HUD can put whatever cap it wants on rolling such costs into a mortgage, officials contend. While the mortgage bankers claim that 150,000 buyers will be squeezed out of the market each year, Weicher estimates that only 20,000 families will be affected.

Democrats will try to craft the FHA rules to their liking. House Banking Chairman Henry B. Gonzalez (D-Tex.) last month called for an audit of HUD's auditors, citing evidence that Price Waterhouse overstated the FHA's financial problems. Even with the increase, housing analysts say the changes won't make a dent in the FHA's default rate. If the stiff terms force the FHA's most creditworthy borrowers to opt for private mortgage insurance, which offers less paperwork and lower premiums, the FHA may wind up taking on the worst risks of all.

By Mike McNamee in Washington

INVESTIGATIONS

NOW, PENSION MANAGERS CAN'T REST ON THEIR ANNUITIES

The Labor Dept. is suing companies that bought shaky contracts

During the 1980s, thousands of employers pulled out of the pension-plan business. In many cases, companies bought annuities to pay the benefits that retirees and workers had already accrued. That enabled the employers to fulfill their obligations.

Or so they thought. Now, the Labor Dept.—spooked by California regulators' seizures of Executive Life Insurance Co.

and First Capital Life Insurance Co.—is serving notice that pension managers must back annuity purchases long after the transaction. First, Labor sued Maxxam Inc. and MagneTek Inc., which bought Executive Life annuities despite warnings that the insurer was unsound. The suits, which the companies are contesting, demand that the employers restore losses by 6,000 beneficiaries. Labor

says it will sue six other unnamed companies if they don't guarantee annuities bought from shaky insurers.

The department is also conducting probes into 60 other companies that may have violated their fiduciary responsibilities in selecting annuity contracts. Those companies may have ignored outside experts' advice or purchased cheaper contracts from a lower-rated insurance company when they had the cash to buy from a better one. Assistant Secretary David G. Ball warns that he plans more lawsuits. "Employers must buy the safest available annuity," he says.

Ball is setting a higher fiduciary standard for the purchase of annuities than for pension investments. The risk to retirees is too great to do otherwise, he says. More than 3 million retirees and their dependents receive annuities purchased by their pension plans from insurers. Unlike pensions, annuities aren't protected by the federal Pension Benefit Guaranty Corp. (PBGC). But nearly 70 life insurance companies, mostly small, failed in 1989 and 1990, according to the General Accounting Office.

SECOND-GUESSING. Not surprisingly, Labor's tough new stance frightens insurers. They're worried about the department's efforts to set minimum standards for choosing annuity providers. "We feel that standards would be the equivalent of providing a list of approved insurers," says Henri R. Bersoux, spokesman for the American Council of Life Insurance.

Pension managers are troubled as well. They fear that their obligation to beneficiaries may never end. They also worry about second-guessing by government bureaucrats. "What is the safest? Does it mean that an employer has to spend more money than it needs to?" asks Howard C. Weizmann, executive director of the Association of Private Pension & Welfare Plans.

If Weizmann is unhappy with the Labor Dept., wait until Senator Howard M. Metzenbaum (D-Ohio) gets done. Metzenbaum, whose labor subcommittee planned hearings on annuity safety, is mulling a measure that would require the PBGC to back annuities. He's also considering requiring companies that terminate overfunded plans to guarantee the annuities held by retirees. "The wheeler-dealer takeover artists of the 1980s terminated those pension plans so they could use the excess funds as their corporate piggy banks," he says.

Metzenbaum and pension managers agree that protecting retirees requires tighter insurance regulation. In the meantime, pension managers are on notice: Fulfilling your obligations to your workers may soon be harder than ever.

By Susan B. Garland in Washington

MARKETING

THE FDA IS GROWLING AT DRUGMAKERS, TOO

It gets tough with companies that promote drugs for unapproved uses

In the go-go 1980s, when regulators slept, drug marketers let their imaginations go. They concocted clever strategies for boosting sales, from advertising prescription drugs directly to consumers to hosting "symposiums" for doctors in exotic locales. One gambit was based on the fact that physicians are free to prescribe drugs for uses not approved by the Food & Drug Administration. Once a drugmaker got the agency go-ahead to sell a product to treat a

moting drugs for nonapproved use (table). Up to a dozen more cases are under investigation. "Promotional practices have, to be blunt, gotten out of hand," Kessler told pharmaceutical company representatives at the annual meeting of the not-for-profit Drug Information Assn. on June 17. "The current excesses must stop."

SIN OF OMISSION. Kessler's message is already sending tremors through the drug industry. "There are many companies that are pulling back from [promotional] programs they were planning to launch," says Jo Scott, chief executive of Scott-Levin Associates, a drug-marketing consultant in Newton, Pa.

Take the case of Ciba-Geigy Corp.'s gallstone-dissolving drug, Actigall. The company's marketing mavens had the idea of advertising in women's magazines and newspapers. But in Kessler's eyes, the ads are guilty of a sin of omission: They don't mention that a new type of minor surgery can often solve the problem in far less time. Ciba-Geigy says it has halted the campaign.

The FDA's strongest actions to date have been taken against industry promotions of unapproved uses for drugs. Such promotion isn't necessarily just a sales-boosting ploy. In treating many types of cancer, physicians depend on drugs approved for other forms of the disease. Half of all cancer drugs are prescribed in this "off-label" way. While these uses may help patients, the law bars companies from promoting or advertising them.

That hasn't stopped drugmakers from trying. Industry experts estimate that more than half of all pharmaceutical companies push unapproved uses. Mar-



TARGETS OF THE FDA CRACKDOWN

Company	Drug Approved use	FDA objects to promoting these uses:
COLLAGEN	Collagen Acne scars	Making lips fuller
JOHNSON & JOHNSON	Retin-A Acne	Combating wrinkles
ICN PHARMACEUTICALS	Ribavirin Respiratory virus	AIDS treatment

DATA: FOOD & DRUG ADMINISTRATION

minor form of cancer, say, it then told doctors about additional studies demonstrating the treatment's efficacy for other types of cancer. Presto: big sales.

Those freewheeling days are coming to an end. Under new Commissioner Dr. David A. Kessler, the once-toothless FDA has a fearsome new set of fangs. In addition to his well-publicized attack on misleading food labels, Kessler is targeting what he sees as questionable advertising and promotion by the drug industry. So far, the FDA has cracked down on a handful of companies that were pro-

ing experts, for example, say that Eli Lilly & Co.'s representatives are quietly sending doctors about new studies showing that Prozac, its popular antidepressant, is also an effective treatment for obesity. These experts also contend that Upjohn Co.'s sales staff is pointing to studies that show the company's baldness drug, Rogaine, will promote hair growth in women, a use not yet approved. Both companies insist that their sales teams are forbidden to mention unapproved uses. So far, the FDA hasn't taken action.

APPROVAL PROCESS. Bristol-Myers Squibb Co. hasn't been so lucky. The company had been sending doctors a magazine, *Oncology Commentary*, which published studies showing that the firm's cancer drugs had lots of nonapproved uses. FDA officials pointedly told Bristol-Myers that the magazine was clearly "promotional literature in the guise of a scientific journal." In a May 10 settlement, the drugmaker agreed to kill the magazine. Johnson & Johnson also fell under the FDA's watchful eye. J&J sponsored a press conference to publicize a study—once shown to be at best inconclusive—demonstrating that its acne drug, Retin-A, also combats wrinkles. The FDA has taken the case to the Justice Dept. to review for possible prosecution for violation of federal drug laws.

The FDA is also taking a look at other common industry practices, such as buying supplements to medical journals or paying for conferences. "What has gone wrong dramatically are promotions that are disguised as something else, such as symposiums that look like traditional medical conferences but are sponsored by the maker of a drug," says Ann M. Witt, head of the FDA's drug marketing office. In 1988, 16 drug companies spent more than \$85 million to sponsor 34,688 symposiums, up from only \$3 million for 175 conferences in 1976.

Critics say the FDA's snail-like drug-approval process is partly to blame for widespread off-label use of drugs. If the FDA bars companies from telling doctors about new studies, oncologists say, cancer patients will suffer. "The FDA should regulate after cholesterol claims on food," says Dr. Gerald P. Murphy of the American Cancer Society. "But if they want to regulate the drug industry, they should get on with their own homework and get drugs approved faster."

Not to worry, says the peripatetic Kessler. The FDA chief says that he's working on a series of measures to speed new drug approvals, and that the results are already being felt. But for companies pushing the boundaries of drug promotion, Kessler is transforming the go-go '80s into the go-slow '90s.

By John Carey in Washington and Joseph Weber in Philadelphia

REGIONS

THE MILE-HIGH CITY IS STANDING A LITTLE TALLER

After a punishing slump, the good times may be about to roll in Denver

As the rough-hewn stomping grounds of silver prospectors and oil wildcatters, Denver has known its share of busts. But even its history didn't prepare the city for these past eight years, as Denver suffered through the worst economic downturn since the Great Depression. Its reputation wasn't helped by the notorious failure of Denver-based Silverado Banking, Savings & Loan Assn., which counted first son and S&L poster boy Neil M. Bush among its board members.

Today, though, Denver is bouncing

No one industry can take credit for the city's turnaround. The single best piece of news though, is that the real estate market has regained its equilibrium, untroubled either by inflated values or a glut of inventory. Even without a spate of easy S&L money, housing starts in the first third of 1991 are up 29% over last year, while the downtown office vacancy rate has fallen to 21% from a peak of 27% in 1987.

So July 1 is not a bad time to be sworn in as mayor. Still, Webb points out, it is not all blue sky for Denver. His first priorities are to help struggling small companies and to attract new business.

Another priority is paying down the city's \$2.6 billion in debt, up from \$576 million in 1983. "We have to find out if we can justify all the economic balls in the air," Webb says. One ball he doesn't like is the \$325 million package of tax breaks and construction financing offered to United to locate its maintenance facility in Denver. He says it's just too costly, though the plant will eventually create 10,000 jobs. United is expected to make its choice by summer's end.

SHOE LEATHER. The new mayor ran a populist campaign. He entered the race in February, backed by just 7% of the voters. While his opponent, District Attorney Norm Early, who is also black, had a \$1

million war chest, Webb spent just \$300,000. His attention-getting ploy: a six-week walk around town, talking to voters and sleeping in the homes of his supporters. He also lost 15 pounds.

Shoe leather is a great gimmick, but it is Webb's pragmatic ideas that got him elected. He makes it clear that he won't be pushing new public-works projects. "It's time to burn the municipal credit card," he says. That's just fine with Denverites, who are weary of the big, expensive projects that came in with high-rolling speculators from out of state.

Among those seeking greener pastures is Neil Bush. He has put his five-bedroom house on the market for \$695,000 and is scouting jobs in Texas. He won't be missed. The 1980s, as Denverites can attest, are definitely over.

By Sandra D. Atchison in Denver, with Kevin Kelly in Chicago



A WINNER: WEBB IS THE CITY'S FIRST BLACK MAYOR

back, and its first black mayor, city auditor Wellington Webb, elected on June 18, stands to reap the benefits. Webb will preside over a city that, in the words of outgoing Mayor Federico Peña, is "prepared for the next century. I'm calling this 'the Denver decade.'"

That's political sloganeering, of course, but some boasting is to be expected. Unemployment is down to 4.6% from 8% in 1987. Just days before the election, Denver, along with Miami, was picked as an expansion city for Major League Baseball. And thanks to generous incentives offered in early June by the city council and the state legislature, Denver is the leading contender among 10 cities for United Airlines Inc.'s \$1 billion maintenance facility. Construction has begun on a \$1.9 billion airport, the first major new airport since Dallas-Fort Worth International Airport opened in 1974.



ST. PETERSBURG'S \$110 MILLION SUNCOAST DOME: THE TOWN IS AGAIN SEEKING A CLUB

HAVE TEAM, MAY TRAVEL

Baseball's weakest clubs may be allowed to decamp for greener climes

When Houston Astros owner John McMullen put his team on the block last November, he set the price at \$95 million, the same price the National League is charging the owners of its two new expansion teams in Denver and Miami. Seems fair. But it may be too steep for Houston. McMullen says he hasn't heard from a single viable bidder in the Lone Star State. He's talking to one out-of-state buyer willing to stay in Houston. But much greater interest has come from cities eager to claim the Astros.

McMullen and other owners eager to cash in their investments can now take heart. At the owners' meeting that ended on June 13, Baseball Commissioner Fay Vincent, saying he was "willing to be persuaded," announced a study of franchise moves. This is no small change for a business where no team has relocated since 1972, when the second incarnation of the Washington Senators became the Texas Rangers.

ADDED VALUE. It's also a risky step for an image-conscious sport. Moving may bail out such troubled teams as the Seattle Mariners (table). But relocation fosters controversy and revives discussions of baseball's antitrust exemption. So it's the last resort for sickly clubs. Thus, there's no thought of moving the Baltimore Orioles, even though they are up for sale.

Relocation is a nearly surefire way to boost an ailing club's value. A franchise such as Cleveland or Seattle might trade for only \$75 million in its home market, says Michael Megna of American Appraisal Associates Inc. But demand for major-league ball so outstrips supply that either team would hear "much more attractive offers from cities that didn't get one of the expansion teams."

Already, the four cities that lost out on expansion are courting the weakest clubs. St. Petersburg-Tampa, which has already sunk \$110 million into building

the Florida Suncoast Dome, kicked off its drive on June 13. In Buffalo, "if there are teams... interested in moving, we want to be at the table talking to them," says Michael J. Billoni, vice-president of Rich Baseball Operations, which led the city's expansion bid. Washington and Orlando are also interested.

Don't expect to see more than a handful of moves, though. "The sentiment [among owners] is that you should stay where you are, unless you have good evidence" that the situation is almost hopeless, says Philadelphia Phillies President William Giles. Vincent has said such evidence might include serious stadium problems, lack of community support, and steady financial losses.

Three or four of baseball's 26 teams might meet that test (table). The Seattle Mariners are the most likely to secede. The team has sold only 5,300 season tickets, second-lowest in the majors. Worst bids for new local-TV rights are a pittance: \$1 million or so, and the team lost \$3 million last year. Principal owner Jerry Smulyan says he remains committed to Seattle, which opened the Kingdome in 1976 for the Mariners, but he needs more business and broadcast support.

DIRE NEED. Conversely, McMullen may not get permission to move from the large, potentially lucrative Houston market. True, the Astros drew only 1.3 million fans last year. But that's mostly because McMullen stripped the team of Nolan Ryan and its other top stars. Says Giles: "They don't have a real justification for leaving."

Less certain are the fates of the Cleveland Indians and the San Francisco Giants. Both are in dire need of new stadiums. Last year, Cleveland-area voters approved new sin taxes to pay roughly half the cost of a new stadium complex, and \$148 million in stadium bonds have already been sold. Stadium backers are now working against a June 30 deadline for agreement on a lease with the team. While the project isn't yet fully financed and talks could still break down, odds are the Indians will stay.

Voters haven't been so agreeable in the Bay Area, rejecting stadium proposals twice in the past two years. But the votes were close, and now both San Francisco and San Jose, Calif., are hatching new ballpark schemes. Giants owner Bob Lurie will stay put at least until late next year.

As Cleveland and San Francisco demonstrate, the threat of leaving often produces concessions. But now that baseball's solons are thinking the unthinkable, some team seems sure to deliver on its threat.

By William C. Symonds in Toronto, with bureau reports



The music world and makers of digital audio tape recorders are ready to call a truce. The two sides have clashed for years over how to compensate artists for lost revenue caused by home copying. That has prompted record companies to stymie the growth of the high-fidelity technology by refusing to provide songs for prerecorded digital tapes.

BUSINESS WEEK has learned that the two sides are about to cut a deal—possibly by the end of June. “We’re closer to an agreement than ever before,” says Tandy Chairman John Roach. Under the accord—which will soon be proposed as legislation—consumer electronics makers would charge an extra 2% to 3% for duplicating gear such as digital recorders, blank tapes, and recordable compact disks. The money would go into a fund for record producers, lyricists, and recording artists.

Consumer-electronics makers had opposed such fees, fearing the increased costs would crimp equipment sales—and would carry over to the lucrative video industry as well. But now they believe that without such a compromise with the recording industry, digital-tape technology may never get off the ground.

Hollywood's material girl is almost certain to get even wealthier. For the past three weeks, Time Warner executives have been wooing slinky superstar Madonna in contract talks that could lead to the most lucrative deal yet signed by any star. The benchmark so far is singer Michael Jackson's \$65 million deal to make records for Sony Music and films for the company's Columbia Pictures unit. Madonna, according to

Like Jackson, she wants a 50-50 partnership on her records, boosting the current 18% of the retail price she collects to nearly 30%. Madonna, who has sold more than 23 million albums for Warner since signing with its Sire Records unit in 1983, would also make films for Warner Bros. The deal would escalate sharply with hits. Last year, Madonna made an estimated \$39 million from her *Blond Ambition* tour, album, and movie appearances.

► The Internal Revenue Service is one step closer to cracking down on foreign companies with U.S. operations for underpaying their taxes. On June 14, the agency issued regulations requiring U.S. distributors owned by foreign companies to keep better records on the prices their foreign parents charge for products and services. They must also report to the IRS on transactions with all foreign companies.

Tax experts believe that the U. S. is losing as much as \$30 billion in tax revenues a year because these foreign companies overcharge their U.S. distributors for products, re-

Golfers put off by the swirling winds and tricky terrain at Pebble Beach should probably forget about the sixth annual Arctic Open. Teeing off at 8 p.m. on June 21 at Iceland's Akureyri Golf Club, the 36-hole tournament is only for golfers prepared to endure bone-chilling temperatures, Arctic wind and rain, and a soggy, muddy course. On the bright side, daylight lasts around the clock, and black so players won't lose track. Certified golf addicts have already

Since the course is only 31 miles south of the Arctic Circle, parkas, not plus-fours, are the uniform of the day. So event sponsor Cross Creek Apparel is outfitting the intrepid duffers in turtlenecks and other gear. But couldn't the company come up with a better tournament logo than the midnight sun over a blue sea? How about a nine-iron encased in ice?



ducing the income the IRS can tax. The IRS will likely face challenges from foreign companies who claim that the new requirements, which don't apply to U.S. companies, violate bilateral tax treaties.

► Columbia Gas System, the \$2.4 billion natural-gas distributor, is threatening to file for Chapter 11 protection unless gas producers agree to renegotiate old contracts. The cash-strapped Wilmington, (Del.) company warned on June 19 that it may be forced

to write off up to \$1 billion in the second quarter. The reason: losses from old pacts with producers at prices far above today's depressed market levels. Tied to these high-priced contracts, Columbia is finding few takers for gas it has to sell for nearly twice the going rate. The write-off could jeopardize the company's credit lines. To conserve cash, Columbia has suspended the dividend on its common stock.

► Procter & Gamble is making a plunge into Eastern Europe. On June 19, P&G became the first U.S. company to buy a 100% interest in a Czech company, Rakona, the country's largest detergent maker. P&G will pay \$20 million up front and at least another \$24 million to upgrade and expand. It has also formed two joint ventures in Hungary to produce paper and personal care products. In another deal, it will sell diapers, shampoos, and detergent in Poland. The push comes none too soon: German detergent maker Henkel has been picking off key Czech and east German properties.





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IT MAY WELL BE BYE-BYE TIME FOR JOHN SUNUNU

Portrait of power ebbing in Washington: It begins with a cascade of damaging leaks. Then come the knowing snickers on the capital party circuit. Soon, the skewered official finds himself the butt of a nonstop stream of cutting jokes from late-night TV comedians. And before long, the President himself is making a pained expression of tepid support for his imperiled aide.

For three high-flying years, White House Chief of Staff John H. Sununu cheerfully maintained that his energy and intellect made him immune to this dour trial. Now, he has stopped smiling.

After weeks of trying to snuff out a spreading controversy over his use of government planes and limousines, Sununu appears to be in serious jeopardy of losing his job as George Bush's iron-fisted enforcer. Sununu has been unable to contain the damage from press leaks about his extensive use of government jets for everything from ski trips to visits to his Boston dentist. He insisted that his lofty position requires that he be in constant communication with top government officials.

INSIDE JOB: The White House slapped restrictions on the staff chief's personal travel. But Sununu responded by hitchhiking rides on corporate jets, a practice that raised a whole new set of ethical questions. And new reports that he continues to use government cars for long-distance personal travel have caused the controversy to flare anew. More ominously for Sununu, the latest incidents have angered President Bush, who is extremely sensitive about his promise to raise ethical standards in government. "Bush has a self-image deeply ingrained in public service," says one close adviser, "and Sununu looks greedy and self-important."

To Sununu's small coterie of die-hard defenders, nothing much is going on here beyond one of Washington's usual rites

of political cannibalism. "This is still an inside-the-Beltway frenzy," says Charles Black, a leading Republican political strategist. "Most people still don't know who John Sununu is." But a number of GOP veterans are coming to believe that the Sununu drama is part of a larger tableau: A life-and-death struggle by longtime Bush aides to foil Sununu's desire to control Bush's 1992 reelection strategy from the White House.

In 1988, this view holds, Sununu's street-fighter approach to politics was perfect for George Bush. This time around, some

Bush veterans worry that Big John's strong-arm tactics will not mesh with the President's desire to float through on a lofty, high-road campaign against weak Democratic opposition. "What's happening to Sununu is an inside job," says a longtime Bush intimate.

HAUGHTY PALS. Some Bush partisans also want to break the powerful alliance of Sununu and Budget Director Richard G. Darman. The pair dominates White House domestic policy. But their hauteur angers Commerce Secretary Robert A. Mosbacher and many other Bush friends in the Cabinet. And it upsets GOP pros, who consider Sununu and Darman policy wonks whose political fumbles hold peril for Bush.

How long can Sununu hold on? If the President decides Sununu is becoming a liability, he won't hesitate to dump him. One sign of Bush's growing concern came on June 19, when he added these telling words to his customary defense of his top aide: "I recognize, and I think the governor does, that there's an appearance problem" in Sununu's limo trip. With a few more endorsements like that, the John Sununu who once terrorized Washington with his imperious ways could soon have more time for travel than he ever dreamed of.

By Lee Waleczak and Douglas Harbrecht



SUNUNU: OBJECT OF A PLOT BY BUSH AIDES?

CAPITAL WRAPUP

DEFENSE

The national outpouring of affection for U.S. troops in the wake of the Gulf War warmed hearts in the Pentagon. But now, Defense Dept. planners fear, the political fallout from success may warp military-spending priorities as the U.S. designs a downsized fighting force for the post-cold-war era. One major concern is that enthusiasm for Desert Storm, combined with some old-fashioned pork-barrel politics, may lead Congress to pour money into unneeded troops and weapons. For example, the House-passed version of the 1992 defense-authorization bill retains 67,420 reserve and National Guard troops

that Defense Secretary Richard B. Cheney wanted cut. And the House defied Cheney by cutting funds for Star Wars and stealth while continuing the Marine Corps' V-22 vertical-takeoff plane and upgrading new F-14 fighters for the Navy.

Cheney is trying to hold the line in the Senate. He has warned Senate GOP leaders that pork-barreling will come at the expense of such Pentagon priorities as the B-2 Stealth bomber and anti-missile defenses. "After every war, the U.S. has downsized [the military] in a strange way," says Senator Richard G. Lugar (R-Ind.), who supports Cheney. "We wind up with a fighting force that isn't the one we need."

THRIFTS

There's nothing Congress guards more jealously than its power of the purse. And nothing it likes less than having to vote every few months to pour billions of dollars into the savings-and-loan cleanup. So distasteful, in fact, has the thrift bailout become that lawmakers are thinking of giving the Treasury Dept. an 18-month blank check. Congress has approved \$78 billion for the cleanup this fiscal year, and Treasury Secretary Nicholas F. Brady is expected to seek \$100 billion for 1992. Lawmakers would prefer not to vote for more S&L spending until after the 1992 elections.

A BIG BUNDLE OF HOT NEW EXPORTS

Japan's latest wave of products will wow overseas consumers—and fatten its trade surplus

Hofu, a port 56 miles west of Hiroshima on Japan's Inland Sea, is best known for an imposing red Shinto shrine where residents pray for success. Late last summer, local employees at one big Hofu employer, Mazda Motor Corp., were saying more prayers than usual, as the U.S. economy headed into recession and war. Roughly two-thirds of Mazda's Hofu output, including the snappy Miata, rolls straight down to the city's sun-baked docks and into the holds of ships bound overseas. As the U.S. outlook darkened, managers and employees braced for production cutbacks.

They never came. Mazda's Hofu and Hiroshima facilities are turning out more new cars than ever. And exports of the Miata are up 30%. While total Mazda shipments to the U.S. slipped 8% last year, the car-maker more than made up for the shortfall with an 18% jump in exports to Europe and increases to Asia. Germany gobbled up Mazdas as East and West reunified, mak-

ing Mazda the top seller of Japanese autos in Germany. And fatter wages in Taiwan and Thailand are fueling Mazda sales there. "The U.S. recession has had no impact on our plants," says Mazda manager Seiichi Inamoto. "A shortage of demand is not our worry."

U-TURN AHEAD? After years of declining trade surpluses with the world, Japan is riding a new export wave. In the first five months of the year, its global trade surplus grew 32.4% and by some estimates will grow by almost that much for the full year (charts, page 42). Like Mazda, other big manufacturers such as Matsushita Electric Industrial Co. and Komatsu Ltd. are shipping more of everything—from camcorders to dump trucks. Runaway demand in Germany has pushed up Japan's surplus with Europe some 66% so far this year. In Taiwan, Thailand, and Malaysia, Japan is selling everything from VCRs to complete factories. Its trade surplus with the entire region was up 49.5% through May.

Japan's export boom is beginning to hit the U.S. as well. That means improvement in the American deficit with Japan could soon make a U-turn. About to roll off Japan's seemingly unstoppable assembly lines is a dazzling array of consumer and industrial gadgets. An entire new generation of products is being readied: Wide-screen TVs, lighter and brighter laptop smarter robots, and hotter cars could become the must-buys of the mid-1990s. And what it doesn't buy as finished product the U.S. buys as components—the building blocks for advanced electronics goods.

What's more, a U.S. recovery will revive demand for Japanese goods, especially consumer electronics. Assuming even a mild recovery in the second half (page 48), U.S. consumers may find it hard to resist Sony Corp.'s new palm-size Data Discman. Instead of playing music, it "reads" 3-inch disks, each holding thousands of pages of text. Or take Toyota Motor Corp.'s sleek high-performance, \$37,500 Lexus SC400.

A NEW GENERATION OF HIGH-TECH WHIZBANGS

From a handheld library to a vacuum cleaner that 'thinks,' Japanese manufacturers are rolling out a slew of attractive new products

▼ RACY SUBJECT: MAZDA TURNED TO ITALIAN CAR DESIGNERS FOR THE SLEEK LINES OF ITS NEW MX-3, COMING TO U.S. DEALERSHIPS THIS FALL

◀ LAPTOP LUXURY: THE TOSHIBA SPARC LT USES THE LATEST MICROCHIP TECHNOLOGY TO PACK WORKSTATION POWER IN A PORTABLE COMPUTER



ports coupe, on sale since June 1. Already, improvement in the U.S. deficit with Japan has slowed. By yearend, predicts Jesper J. Koll, economist at S.G. Warburg Securities (Japan), the U.S. deficit with Japan will be up 5%. "Japan makes what Americans want," Koll says, "and they'll be buying again."

Tokyo's cautious management of its domestic economy isn't helping, either. The bank of Japan is keeping interest rates high, dampening consumers' appetites for flashy foreign cars and Western art masterpieces and prodding some manufacturers to look abroad for growth. And high growth numbers for the first quarter diminish prospects for an imminent rate cut.

SMALL CHANGE. Any slippage on the U.S. trade front, combined with mounting competitive pressure on auto and computer makers, would come at an awkward moment. The Bush Administration has tried to soothe U.S.-Japanese irritations in the wake of the gulf war and has signed a rapid-fire series of agreements to defuse trade spats. Moreover, with an election year looming, the Administration doesn't want to be tarred by Democratic hopefuls for having failed to manage Japan. So far, U.S. Trade Representative Carla A. Hills is withholding judgment: "There has been some improvement but [no] fundamental change," Hills says.

It wasn't supposed to be like this. Beginning in 1985, Japan's industrial trading partners engineered a dramatic increase in the value of the yen in order to slash Japan's trade surpluses. The surprise now is that Japanese exporters have adapted

thoroughly. A decade of heavy capital spending and technological advance has made Japan dominant in such things as high-volume computer chips and office equipment. Nor have barriers to its market fallen, complain many U.S., European, and Asian manufacturers, despite inroads by the likes of Apple Computer Inc. and Eastman Kodak Co. Although imports kept rising, they couldn't counter the export flow.

Japanese trade officials point to an insatiable appetite for imports in the U.S. as new technologies overtake the old

So, "the trade-adjustment process is over," says Osaka University Professor Iwao Nakatani. "Japan's trade surplus will expand this year. It's inevitable."

Japan's export machine has become much more sophisticated over the past decade. Besides mastering hot new technologies, Japanese companies have invested \$200 billion offshore as of 1990, giving them platforms to make many lower-technology, older products. Meanwhile, at home, they have concentrated on developing more technology-intensive products, in strong demand overseas. Rather than merely exporting cars or VCRs, as they did in the mid-1980s, the companies' export mix includes more capital goods and components, and their products are reaching markets from Japanese factories in many different countries. Toyota and Mitsubishi

Motors Corp., for example, increasingly export parts to Europe and North America from Thailand. Likewise, Japanese companies have begun shipping to Europe cars they make in the U.S. Measuring country-to-country trade gaps with Japan has become vastly more complex than before.

PUSH AND PULL. Japan's officials say they tried hard to chop their chronic trade surpluses. They cut interest rates in the mid-1980s to spark domestic spending that would soak up Japanese products and draw in more imports as well. But the plan worked too well, overheating the economy, and import growth has now fallen off as money has tightened again. Still, government forecasters say the year's trade imbalance will end up flat, at 1990 levels.

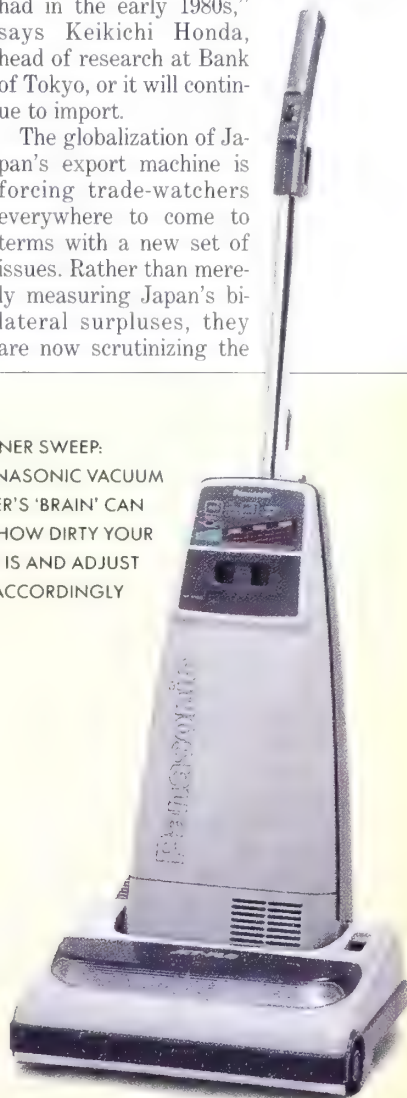
Frustrated trade officials also point to an insatiable appetite for imports in the U.S.—and now in Europe and Asia—as new products and technologies overtake the old in faster and faster cycles. Japan's growing exports aren't just part of a push, say Tokyo trade-watchers. A pull is at work, too. As for the U.S., it "must regain the edge in productivity and technology it had in the early 1980s," says Keikichi Honda, head of research at Bank of Tokyo, or it will continue to import.

The globalization of Japan's export machine is forcing trade-watchers everywhere to come to terms with a new set of issues. Rather than merely measuring Japan's bilateral surpluses, they are now scrutinizing the

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International Business

composition of its trade, whether Japanese goods are made in Japan or in third countries, and just how much local content is actually in goods produced offshore.

Some U.S. critics, for example, are charging that America's improved trade picture with Japan in the late '80s wasn't quite what it seemed. Japan's surplus with the U.S. fell 16% in 1990, to \$41.1 billion, 27% below its 1987 peak. But Kevin Kearns, of the Economic Strategy Institute in Washington, estimates that one-third of the \$15 billion improvement in the U.S.-Japan trade imbalance since 1987 results from Japan's increased purchases of such commodities as fish and paper. Growing exports of "scrap metal and paper don't give us much hope for America's future," says Kearns.

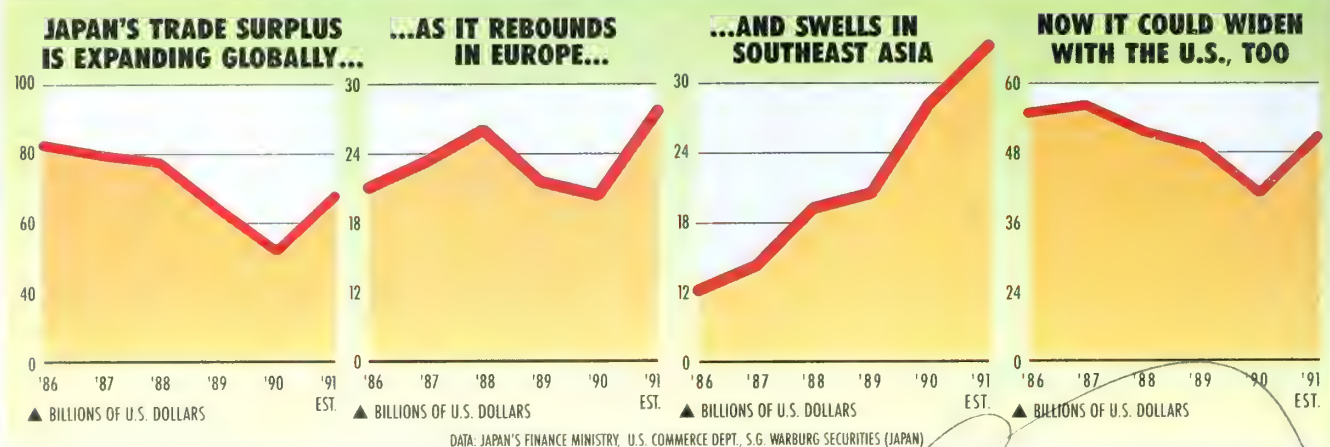
In key sectors such as autos, Japanese

If auto-parts imports are a problem in the U.S. in the midst of a recession, just wait until spending picks up, warn economists. Sales of Japanese-built cars may have fallen off some 20% in the first quarter of this year, but analysts at Merrill Lynch Inc. expect total U.S. sales of new cars and trucks to rebound from 12.7 million vehicles this year to 15.7 million in 1993. Japanese manufacturers will try to meet the increase in demand by raising production at their U.S. facilities. "But they don't have enough capacity to meet that sort of demand and maintain their market shares," says Merrill Lynch Japan analyst Benjamin J. Moyer. "Exports to the U.S. will increase."

The strong appeal of a new generation of Japanese cars seems certain to guarantee that. Aside from such luxury brands as

plunged into minisupercomputers, once the preserve of small American players such as Convex Computer Corp. And Japanese computer makers are exploring ways of boosting power through massively parallel computing.

In office equipment, Canon Inc., for one, is creating smart machines that will use digital technology to squeeze functions performed by fax machines, copiers, and computer printers into one unit. Toshiba Corp. and others are perfecting hospital data systems that will enable doctors to store and retrieve X-rays and other visual material, including CAT scans, from optical disks and transmit the data between hospitals. While U.S. rivals Eastman Kodak, Xerox Corp., and others are working on similar products, they rely on the Japanese to supply most of the parts.



transplants are the focus of renewed attention. Often their parts suppliers follow them, and the U.S. auto-parts industry fears more such inroads. True, U.S. suppliers have quadrupled their sales to Japanese auto makers since 1985, to \$9 billion. But the Auto Parts Advisory Committee, an industry group that advises the U.S. Commerce Dept., warns that the U.S. deficit with Japan in auto parts could double by 1994, to \$22 billion, partly because of the buying practices of Japan's offshore operations.

A case in point: The committee estimates that as of 1989, only 20% of the components of Honda Motor Co.'s U.S.-built Accord was actually procured from domestic suppliers. Honda imported 48% of the parts, according to the study. Japanese-owned suppliers in the U.S. and Honda itself provided the rest, about one-and-a-half times as much as did U.S. suppliers. Honda disputes the figures, saying that the Accord's local content, including labor, has risen steadily, to 75% now, up from 65% in 1989. Honda is also under fire by the U.S. Customs Service for allegedly inflating the percentage of North American components in cars built in Canada.

Toyota's Lexus and Nissan's Infiniti, new models like the well-appointed Mitsubishi Diamante are rolling onto dealer lots. Mazda's hit Miata will be joined this fall by a sleek sports car with Italian styling, the MX-3. The introduction of new Japanese models is hitting Detroit across most of its product range.

SNOOP-PROOF PHONES. Autos are only part of the picture. With more money in their pockets, U.S. consumers will be itching to buy the latest arrivals in Japanese home entertainment and office equipment. One sure seller is the Sony Data Discman, likely to be priced at less than \$500. And Sharp Corp. and Kyocera Corp. are making snoop-proof cordless phones. The new phones, at about \$380, could catch on quickly. In computers, Fujitsu Ltd. has

What's remarkable about Japan's new export momentum is that the U.S. hasn't dominated center stage the way it once did. Once dependent on the U.S. for nearly half of what they sold overseas, Japanese companies logged 34% of their export sales in Asia in 1990. Sales to North America slipped to 36% in the same period. This year, Asia may take the lead. "Japan has successfully diversified its export-trade risk away from North America," says Paul A. Summerville, economist at Jardine Fleming Securities Ltd. in Tokyo.

That reduced dependence on the U.S. may be one reason Japanese officials are increasingly confident in arguing that the trade imbalance is an American or European problem. An upturn in Japanese exports, they say, isn't just Japan's doing. Americans, Europeans, and Asians are all hooked on what Japan makes, from Canon printers to red Miatas. If that argument carries the day, the workers down in Hofu won't have to spend so much time saying prayers at their shrine.

By Ted Holden, with Neil Gross in Tokyo, Dirk Bennett in Taipei, James B. Treece in Detroit, Paul Magnusson in Washington, and bureau reports

'Japan has successfully diversified its export-trade risk away from North America'

ASSEMBLY LINES START MIGRATING FROM ASIA TO MEXICO

Manufacturers are shifting operations in anticipation of a free-trade pact

Soon, a lot more of that outdoor gear in your closet may come from Mexico instead of China. That's the message from Bill Simon, managing director of Odyssey International Ltd., which for years has been producing a wide range of garments and sporting goods for Lands' End, L.L. Bean, and North Face in China. Now, he thinks that Mexico may have advantages over China and other Asian countries as a manufacturing site to serve the U.S. market. "Mexico is fertile ground for us," he says. "We'll have three more plants there by the end of this year."

He has plenty of company. Throughout the 1970s and 1980s, thousands of U.S. companies farmed out contracts to cheap labor mills throughout Asia. But now, with Mexico trying to negotiate its way into a North American free-trade zone and China's relations with Washington souring, U.S. manufacturers are starting to bring their operations back home to North America.

The shift could prove an unforeseen boost for U.S. businesses. The new plants will rely heavily on stateside suppliers. Already, the Mexican operations of U.S. companies ranging from chemical giant Du Pont Co. to SCI Systems Inc. of Huntsville, Alabama, which has a computer-component plant in Guadalajara, are gearing up for higher demand.

Leading the rush to Mexico are electronics and garment companies, which now want to be just a stone's throw across the Rio Grande from the U.S. market. They are setting up *maquiladoras*—assembly plants on the U.S.-Mexico border. Rather than expanding an existing plant in Singapore, American Telephone & Telegraph Co., long established in Mexico, is scheduled to open a 500-employee answering-machine factory in Guadalajara in July. AT&T is also moving its cordless-phone-repair operation to Mexico from Singapore, thinking that the shorter distance will speed up customer service.

POLITICAL HEDGE. The first port of call for the industrial émigrés is usually Tijuana and its U.S. neighbor, San Diego. *Maquiladora* consultants in the area, who for a decade have been helping to

move U.S. companies from the Rust Belt states to the border, are now doing a booming business bringing in American clients from Asia. "We're in the midst of moving 2,000 jobs from China to Mexico," says Randy Marks of Inter-American Holdings Co.

Some companies have turned to Mexico to fill changed production requirements. Proxima Corp., a private San Diego company that used to do most of its

U.S. revokes China's most-favored-nation status, he says, the company would likely close down 70% of its China operations. At \$8 a day, Mexicans earn two to three times the Chinese rate, but Odyssey values Mexico's proximity to the U.S. market. He also thinks Mexican labor costs will be roughly the same as in Malaysia, where he also has several plants. "I feel a bit of a fool for not having been more aggressive with Mexico before this," he confesses from his Hong Kong office.

TAIWANESE BIKES. Many Asian businesses are also pouring money into Mexico. In the searing heat of Mexicali, Taiwanese entrepreneur Lawrence Chu is opening up a *maquiladora* park called Ac-mex. Chu foresees his countrymen moving in to make baseball caps, furniture, and bicycles. On the Yucatan Pen-



ODYSSEY'S PLANT IN MEXICO: MALAYSIA-LIKE WAGES AND NEARER TO THE U.S. MARKET

manufacturing in Taiwan, built a factory in Tijuana just down Route 5 from headquarters when it switched to producing video projection panels. "We save 30 days on the boat," says Fred Parker, a vice-president. "And if they run into a technical problem at the plant, we can send someone down in a one-hour drive."

For Odyssey, says Simon, the shift to Mexico, where he now has one plant, is in part a political hedge. Odyssey has 65 contract manufacturers in China. If the

insula, 2,000 miles to the southeast, Hong Kong textile manufacturers Lawrence and Kenneth Fang, who supply Liz Claiborne Inc. and Ann Taylor lines, are setting up an \$8 million plant in Mérida. And Hong Kong's Tin's Industrial Co. is moving part of its toy division from China to Mexico.

Mexico is not the answer for every manufacturer. The lack of a strong base of local suppliers can still make sourcing harder there than in Asia. What's more, Western manufacturers will need to have some plants in the Far East to serve the booming markets there. But unlike a decade ago, when practically all the offshore manufacturing was sailing to the Asian Rim, the Pacific Ocean is now a two-way street.

By Stephen Baker in Tijuana and Dinah Lee in Hong Kong, with Peter Coy in New York

The shift is in part a hedge against the possibility of China's losing most-favored-nation status



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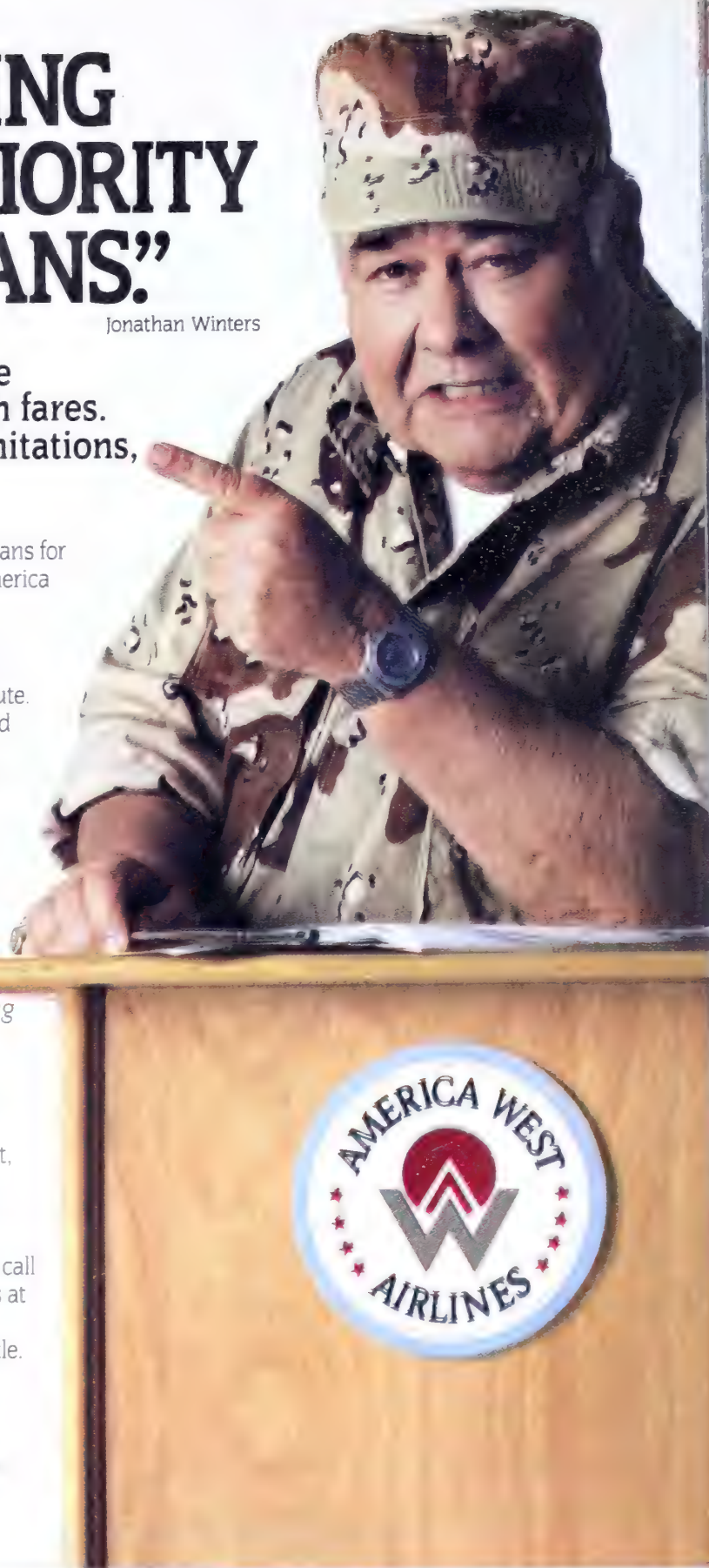
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NORTH KOREA: IF YOU CAN'T BEAT 'EM . . .

It has been the longest, most bitter standoff of the cold war. For 41 years, North Korea's bellicose Marxist regime has clung to the belief that it could dominate the Korean peninsula by force or subversion. Instead, stunning reversals in recent weeks by the North's dictator, Kim Il Sung, show that South Korea is gaining the upper hand—mainly because economic power is driving political wedges between the North and its allies.

On May 28, North Korea announced that it will apply for separate membership in the United Nations, acknowledging for the first time the legitimacy of South Korea. That move came after Kim's two staunchest allies, China and the Soviet Union, did U-turns and supported the South's own bid for a U.N. seat. Then on June 6, the North said it would sign an agreement to let the International Atomic Energy Agency inspect its nuclear facilities. That was a backdown from the North's long defiance of outside political pressures. "The moves represent a de facto admission by North Korea that the game is up," says Daryl M. Plunk, a Korea specialist at Washington's Heritage Foundation.

The North's retreat is a major victory for South Korean President Roh Tae Woo. Behind the big win is Roh's growing skill at combining high-stakes diplomacy with the North's economic prowess. The Soviet Union and North Korea's former East European allies have already established diplomatic relations with Seoul and are expanding economic links. With China, South Korea expects to ratify already-flourishing trade ties by signing an economic pact soon and follow up with diplomatic relations in 1992. To avoid complete isolation, the North now sees little alternative but to seek long-shunned Western ties. It has started trading coal and other products with South Korea, and by fall it is expected to resume the

meetings of Prime Ministers that began in 1990. With such gradual openings, Kim Il Sung, 79, may hope to smooth the transfer of power to his son and successor, Kim Jung Il.

How to exploit these breaks in the North-South deadlock will be a major theme of talks between Presidents Roh Tae Woo and George Bush when Roh visits Washington on July 2-3. Washington remains wary of Kim Il Sung, but if he does sign an IAEA accord, the U.S. may ease its embargo on trade with the North.

JOLTED. Meantime, Roh is in a strong position to push for further improvement in relations with the North and to lay the groundwork for eventual reunification on his terms. South Korea's economy is booming again, and Roh's governing Democratic Liberal Party was expected to make a strong showing in city and provincial elections on June 20. After the two Koreas join the U.N., Seoul may launch a diplomatic campaign to replace the 1953 armistice with a permanent peace treaty.

Hopes for eventual reunification have been jolted, though, by Germany's unification problems. Cost estimates for reunifying Korea range up to \$120 billion, and Seoul's leaders worry about an influx of jobless millions from the North. "The German experience shows that an intermediate stage is necessary before unification of the two Koreas," says Deputy Prime Minister Choi Gak Kyu. South Korean businesses would prefer an interim period of

reforms in the North that would allow them to trade and invest.

Some analysts say reunification could start in five years, although Seoul officials are aiming for the year 2000. Whenever it happens, as in Germany, the successful democratic society will have to pay for the rescue of the Marxist failure.

By Laxmi Nakarmi in Seoul, with bureau reports



A KIM IL SONG MONUMENT: HIS ALLIES ARE DESERTING HIM

GLOBAL WRAPUP

SOVIET UNION

Is Eduard A. Shevardnadze tossing his *shapka* into the ring? The former Foreign Minister may be angling to replace Mikhail Gorbachev as the Soviet Union's President. Observers say that could be one motive for Shevardnadze's mid-June call for creation of a strong democratic party to challenge the Communist Party. He resigned last December with a warning against a "coming dictatorship," and he would be a likely opposition candidate.

Shevardnadze's proposal was swiftly condemned by the Communist Party, but it won support from leaders of Democratic Russia, a loose group back-

ing reformers such as Russian Republic President Boris N. Yeltsin and Moscow Mayor Gavrill Popov. A proposed new treaty of federation would lead to a direct presidential vote by late 1992. Other possible contenders for Gorbachev's job: Kazakhstan President Nursultan Nazarbaev, Leningrad Mayor Anatoly Sobchak, and Yeltsin. Now, all the Soviets need is the equivalent of Iowa or New Hampshire to get the candidates off and running.

EUROPE

The Patriot's stunning success in the gulf war left many Europeans with missile envy. Now, they plan to compete against upgraded Patriot and

Hawk missiles, both built by Raytheon Co., with their own antimissile program. Eurosam, a consortium of France's Aerospatiale and Thomson-CSF and Italy's Alenia, hopes to replace 40 batteries of aging Hawk missiles in France, Italy, and Spain. The tab could hit \$4 billion. An additional 275 batteries in Europe, the Middle East, and Asia are a potentially huge market.

Eurosam's big advantage may be its flexibility. Although the Patriot demonstrated a crude antimissile capability, it and the Hawk were designed primarily to attack aircraft. Eurosam variants will be designed to chase up to 10 incoming missiles at a time—and fire from either land or sea.

COMPANIES ARE
HIRING AGAIN...

HOME SALES
ARE REVIVING...

ASSEMBLY LINES
ARE REVVING UP...

A STRONG RECOVERY?

YES, IT'S POSSIBLE. HERE'S WHY



Manufacturing

Whirlpool's Clyde (Ohio) washing-machine factory, the biggest in the world, has its work force back to nearly full strength

CONSUMERS ARE
SPENDING MORE...

INFLATION IS
MODERATING...

CAR SALES ARE
CLIMBING...

You may not feel it yet, but the U.S. economy is springing to life. The signs are appearing across the country. Ask LTX Corp. President Graham C. C. Miller in Westwood, Mass. Last year was tough for his \$143 million maker of microchip testers, as operating profits tumbled \$17.4 million into the red. But in the most recent quarter, sales soared 38%, and profits rose to \$3 million. Now, the company is adding new employees. "It snapped back very quickly for us," says Miller.

Miller's is not a voice in the wilderness. Harley-Davidson Inc. recently reinstated a five-day workweek at its recreational-vehicle plant in Wakarusa, Ind., and hired back 100 laid-off workers. At Target Corp., the giant discount retailer based in Minneapolis, Minn., same-store sales were up 5% in May over the previous year. Retail sales in the *Los Angeles Times* have increased in the past three weeks—the first glimmer of hope on that front in many months, says publisher David Lanthorn. And permits for new housing construction nationally are up by almost 10% in April and May.

CAUTIOUSLY OPTIMISTIC. The recession is fast becoming history. But what sort of recovery is taking shape? Most economists predict a joyless rebound: slow growth, few new jobs, and a long struggle to work off the financial excesses of the 1980s. The consensus forecast calls for under 3% growth in the first year of recovery, far less than the usual 6% spurt after a recession ends. Others are more pessimistic. "The recovery

should be weak and may not be sustainable," says Allen Sinai, chief economist at Boston Co. (box, page 54).

Yet the rebound now gathering momentum could turn out to be surprisingly powerful. The evidence from past business cycles shows that the deeper the downturn, the sharper the bounce-back—and this recession has been nastier than advertised. Official statistics indicate that the gross national product declined at a 2.1% annual rate over the past two quarters. But the government now says that, come November, a major benchmark revision of GNP data will show a drop that's one-third bigger. And according to DRI/McGraw-Hill, even the government's new numbers will under-

state the decline. Using the most recent price data, DRI puts the rate of decline at a stunning 3.5%. What's worse is that with U.S. net exports on the rise, demand in the domestic economy was shrinking even faster.

The numbers already suggest that most economic sectors have been put through the wringer. Companies have staged one of the sharpest inventory liquidations in history, slashing stocks at a \$31 billion annual rate. Consumers have actually cut their spending by 1.2%, adjusted for inflation, a steeper decline than even that in the severe 1981-82 downturn.

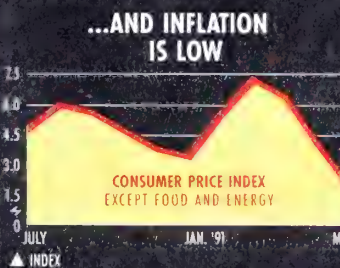
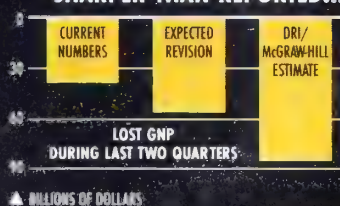
The job picture has been much uglier than the one painted by the unemployment rate, which has been held down by slow growth in the labor force. Unemployment has stayed below 7%, far lower than in the early 1980s. Yet, according to the Conference Board, one household in five had a member who lost his job during the past year. That's what has made this downturn so punishing to so many people, even as the economists kept insisting that it was mild and relatively harmless compared with previous recessions.

ANEMIC. And to get the full measure of this slump, you have to remember that the economy scarcely grew at all in the 18 months before the recession officially started a year ago in July. From the beginning of 1989 until mid-1990, real GNP expanded at only a 1.2% annual rate. And that anemic performance shows up in almost every economic indicator. Housing

THE ELEMENTS THAT MAKE FOR A ROBUST REBOUND



THE DOWNTURN HAS BEEN SHARPER THAN REPORTED...



DATA: COMMERCE DEPT., BUREAU OF LABOR STATISTICS, FEDERAL RESERVE BOARD, DRI/McGraw-Hill, BW



starts have lagged behind new household formation and replacement needs since 1989, factory employment has been falling since February, 1990, and average weekly earnings, adjusted for inflation, have dropped 4.1% since the beginning of 1989.

It's this steep and broad-based decline that is setting the stage for the first act of a strong recovery. Recoveries feed on themselves, much like recessions in reverse: With consumers starting to spend again, businesses quickly rebuild shrunken inventories by stepping up production and hiring more workers, giving consumers more money to spend, and so on. This cycle could easily generate 4% to 5% growth for at least a couple of quarters. Nor will strong growth end there. Rising exports, increased capital investment by business, and low inflation could prolong the robust expansion into 1992 and beyond.

Consumers have already started to spend. Retail sales jumped by a full 1% in May. Auto sales have picked up smartly in the past few weeks. Clothing stores are reporting an upturn in business. And that may be just the beginning. According to the Conference Board, fully one-third of all households delayed major purchases because of the recession. In California, sales of taxable nonfood items have dropped by a stunning 20% in the past year, says David G. Hensley, director of the Business Forecasting Project at the University of California at Los Angeles. "We got clobbered."

Retail sales

At K mart, same-store sales of the giant discount retailer jumped 8.5% in May over the previous year

So consumers around the country have a lot of ground to make up in the initial stages of the recovery. They have been waiting for better times before purchasing a new automobile or the latest electronic gadget. Take Marti Sullivan, a San Francisco fund-raiser for a private school. After six months with a closed checkbook, she bought clothes and shoes for her two children and a new television for the family. "My husband and I joked that we were doing our part to help in the economic recovery," Sullivan says.

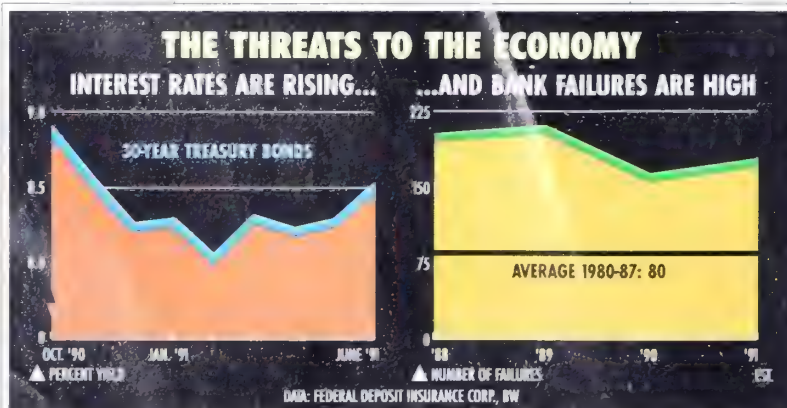
Consumers are even springing for the biggest-ticket items of all: new houses, and all that goes in them. "People can finally sell their homes and move up," says David M. Weekley, president of one of the largest builders in Houston. And that's good, because a small uptick in house sales can have a dramatic impact on the rest of the economy.

Whirlpool Corp.'s Clyde (Ohio) washing-machine factory is the world's largest. Over the past two months, the plant has hired back 340 people, bringing its work force nearly back to full strength. Better yet, production has jumped 15% and in the past two weeks the company has begun scheduling overtime.

Indeed, in most industries it won't take much of a spending increase to spark an inventory rebound. In past recessions, businesses waited too long to cut production, which left them with large inventories of unsold goods. This time, they reacted to falling demand faster than ever before. That means a pickup in demand, notes Daniel J. Meyer, chairman of machinery maker Cincinnati Milacron Inc., "will start flowing through the production system pretty rapidly."

FAST CLIP. And that goes double for the depressed car industry. Although auto sales have been a disaster in the first half of the year, dealer lots are not full of unsold cars. Instead, auto makers slashed production dramatically, taking their pain up front. Now, as new-car sales rise, auto makers are ready to re-up assembly lines for the rest of the year. "We're planning on a good fourth quarter," says John G. Middlebrook, Pontiac Division general manager and General Motors Corp. vice-president. "We're setting good heavy production schedules."

The bounce-back from revived consumer spending and inventory rebuilding should take the economy into 1992.



a fast clip. That's when the second act of the recovery must kick in, and, like at I, it is probably going to be happier in the one written by consensus forecasters. U.S. exports should surge. Exports have remained strong even with major trading partners as Britain and Canada mired in deep slumps. But now there are signs that the global economy is reviving (box). And many American manufacturers are low-cost, highly efficient international competitors these days. "Once the rest of the world lets itself get off, U.S. export business could boom," says Stephen H. Axilrod, vice chairman of Nikko Securities Co.

Business investment will probably pick up off also. To remain competitive, companies are likely to spend strongly on new plant and equipment. Investment has been hit hard by the downturn, with spending on noncomputer equipment and machinery down by 11%. But as the recovery takes hold, rising corporate profits could generate the funds for increased investment. "Many corporations are deferring capital spending now," says Richard B. Berner, an economist at Monom Brothers Inc., "but once they are convinced they have the cash flow to finance capital spending," they will be putting money into new plants and equipment.

SPENDERS? Indeed, the recovery of 1992 could be driven by strong capital investment, rather than a consumption surge. And this investment is likely to be spread to the long run. For example, Milwaukee heavy-machinery maker, is planning to increase capital spending up to 10% a year in the next five years. Says Henry L. Jordan, chief economist at First Interstate Bancorp in Los Angeles: "I've been doing this for 25 years, decades of lapsing confidence, and no business leader wanted to talk past a year or two. Now, they are beginning to talk about a decade."

The biggest spenders may not be manufacturers. Instead, it's service-sector companies in retail, finance, and business services that are being forced to modernize in order to remain competitive, at the same time many are slashing work forces and even losing money. H. Macy & Co., which lost \$101 million in the quarter ended May 4, expects to invest \$180 million in 1991, 40% of that for new technology. And accounting and consulting giant Arthur Andersen & Co., which is still growing, is planning to spend at least 15% more for technology this year. "Underspensing comes back and affects your reputation for quality and service," says Larry A. Weinbach, senior firm's chief executive. Overall, service-sector businesses intend to spend more in 1991 than they did in 1990, according to the Commerce Dept.'s

SUDDENLY, THE GLOBAL SLUMP IS A GLOBAL REVIVAL

Only a few months ago, the outlook for economic growth overseas looked grim. West Germany was struggling with the hefty cost of absorbing east Germany, Britain was mired in a severe downturn, and there were even fears that mighty Japan was sputtering. The global slump threatened to depress demand for U.S. exports, which would have lengthened the U.S. downturn and dampened the strength of any recovery.

But even as the U.S. pulls out of its own slump, the outlook for much of the rest of the world is also improving. On June 18, for example, the Japanese government announced an astounding 11.2% annual growth rate for the first quarter. And the prospects for Germany are looking better, too. "We all have grounds to be more optimistic about the world economy than a year ago," says outgoing Bundesbank President Karl Otto Pöhl.

Recent forecasts have predicted that the major European economies, which account for one-third of U.S. exports, should grow by 2.8% in 1992. That's a sharp improvement over this year's 1.5% rate, says Jonathan Hoffman, senior European economist with Crédit Suisse First Boston in London. The Organization for Economic Cooperation & Development, the Paris-based think tank for 24 major industrialized nations, is predicting that total growth in the OECD countries will top 3% in 1992.

STRENGTH IN UNITY. The most pleasant surprise is Germany, Europe's largest economy. Conventional wisdom has been calling for a slowdown in the second half of 1991 as consumers get hit with tax increases to help pay for reunification with East Germany. But strong wage and employment growth and the boost to incomes should largely offset the tax hikes, say many economists. As a result, Germany could end up with a respectable 3% growth this year. And next year, even if west Germany slows down, east Germany is expected to stage a healthy rebound. After a 15% decline in production this year, it could grow by as much as 5%,

ensuring 3% growth for unified Germany in 1992.

Britain, an important U.S. trading partner, should see an end to its deep recession before yearend. The housing market is improving, and inflation is at its lowest level in three years. What's more, falling interest rates, down from 15% in October of last year to 11.5% now, "should begin to restore a bit of confidence" says Andrew Harrison, group finance director at Courtaulds Textiles PLC, the London-based textile company.

France, too, is seeing the first signs of good news. The French economy has been flat since the end of 1990, but industrial production surged 3.2% in April. The latest business survey by the Bank of France says order books in the automobile and intermediary-goods industries were slightly fuller in May than in April.

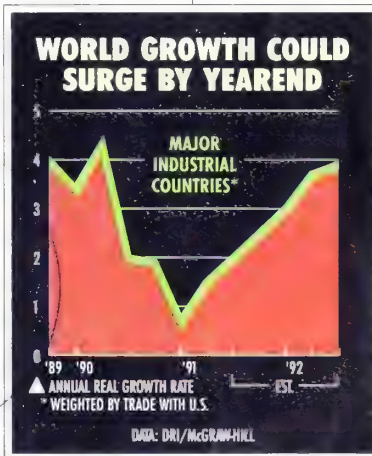
SLOW CLIMB. The services sector is picking up, too. Henri Martre, chairman of French state-owned Aerospatiale, one of the manufacturers in Airbus Industrie, is encouraged by reports that civilian air traffic was back to

year-earlier levels in the second week of June, after being down by roughly 30% since the first of the year. "We have touched bottom, and we are already beginning to climb slowly," says Michele Dèbonneuil, chief economist with Banque Indosuez in Paris.

Looking further ahead, inflation is declining in most European countries, giving leeway for central bankers to cut interest rates. And the economic revival of Latin America, along with the pending creation of a North American free-trade zone, could give a further boost to U.S. exports.

To be sure, the U.S. trade deficit has started to rise again as the domestic economy improves. But even as U.S. consumers and businesses buy more imported goods, they are stimulating overseas growth, which in turn becomes a plus for U.S. exports. In the game of foreign trade, global growth is a win-win proposition.

By Blanca Riener in Paris, with John Templeman in Bonn and bureau reports





April-May survey of capital-expenditure plans. That number has risen since the January-March survey.

What could stall the recovery? The Federal Reserve could tighten the monetary screws if policymakers believe a stronger-than-expected rebound would spur inflation. Already, bond-market investors, spooked by a whiff of good news, have driven up long-term bond rates to 8.5% in May from 8.2% in June. "A modest recovery, rather than a rip-roaring one, is more consistent with where we are and where we want to be," says one Fed official.

LOTS OF LABOR. But core inflation has been abating (chart). Large companies have been forced to cut prices in order to maintain high volume. For example, Ralph Lauren's Womenswear division boosted its sales of fall merchandise by 20%, but only by lowering its prices by 25%. And small businesses have also slashed prices to survive. In Chelmsford, Mass., Stephen Scomis, a 37-year-old carpenter who owns a home-remodeling business, has managed to keep working steadily over the past year by cutting his rates dramatically. Bit by bit, this downward pressure is chipping away at inflation. "My sense is that we're better off on the inflation front than most people think," says Edward G. Boehne, president of the Federal Reserve Bank of Philadelphia.

Housing

Consumers are even springing for the biggest-ticket item of all: A new home. And housing permits are up almost 10%

There's no sign that prices are going to take off anytime soon. Commodity prices are down, and increased foreign competition is limiting the price increases that U.S. companies can make stick. Nonoil import prices rose by only 2.2% during the last year. Even service-sector inflation is cooling down. Since last summer, the annual rate of service-price increases has fallen from 7.5% to 2.5%. Best yet, medical cost inflation is finally moderating, dropping from 10.3% to 7.1%. Says Samuel Kahan, economist at Fuji Securities Inc.: "It's back to the 1950s. The downtrend in inflation is not just cyclical, but structural."

One important force that's holding down wage pressure is the new vulnerability of white-collar workers to layoffs. Service-sector companies are saving money by paring expensive workers and substituting technology. Even after the recovery is in full swing, more white-collar job losses are in the cards, as companies attempt to boost productivity. In banking, for example, the recent merger between Citizens & Southern Corp. in Atlanta and Sovran Financial Corp. in Norfolk, Va., will cost 1,200 workers

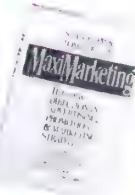
their jobs. Similar layoffs will follow around the country as the industry consolidates. Big law firms are also shedding jobs. "It's a very different ball game for a service sector that has been insulated from competition," says Stephen S. Roach, economist at Morgan Stanley & Co. "Structurally, we could have a tough problem with unemployment in the 1990s."

But for the economy as a whole, higher-than-usual white-collar unemployment is not all bad. There are going to be enough educated workers to sustain an economic expansion. With productivity rising in the service sector, the economy can grow faster without overheating. And there won't be any pressure for a wage-and-price spiral, which is traditionally triggered by labor shortages.

A stronger-than-expected recovery should even help relieve some of the problems lingering from the 1980s. True, the arithmetic of too many empty offices, too much debt, and too many state and local governments in fiscal turmoil will temper the recovery. But growth can salve many wounds. A bounce-back in housing, for example, could strengthen the loan portfolios of weak banks. The Federal Deposit Insurance Corp. estimates that 180 banks could fail this year if the economy rebounds by midsummer. If not, 230 banks could go.

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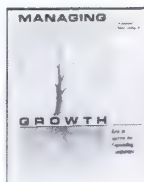
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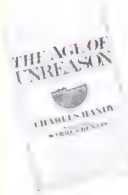
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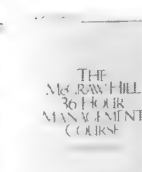
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and local government budget gaps is a healthy economy. Consumers spend, and sales-tax receipts rise. Incomes improve, and so do income-tax payments. Meanwhile, local government expenditures for unemployment insurance and for welfare fall.

To be sure, households and businesses are still burdened by a lot of debt. But household borrowing has slackened, and

companies have been issuing new equity at near-record levels to get their books in better financial shape. Debt will become less onerous, too, as recovery allows both sectors to service their borrowing more easily.

The consensus forecast believes in a weak recovery, despite the spate of good economic news. Says the Federal Reserve's Boehne: "Every recovery is fore-

cast to be slow, sluggish, modest, even anemic." Judging by past experience, odds are that the consensus will be wrong again.

By Michael J. Mandel and Christopher Farrell in New York, with Gary McWilliams in Boston, Mike McNamee in Washington, Kevin Kelly in Chicago, Laura Zinn in New York, and bureaus reports

RECOVERY—OR A ROLLER COASTER?

Retailers are busier, and so are homebuilders. Payrolls are expanding, and production levels are on the rise. All this upbeat news means the recession is over, right?

Not everyone is convinced. Some economists caution that it's too early to pop open the Dom Perignon. Instead of a recovery, these bears warn, the economy will experience a "double-dip"—that is, after rebounding in the second quarter, gross national product will once again head south.

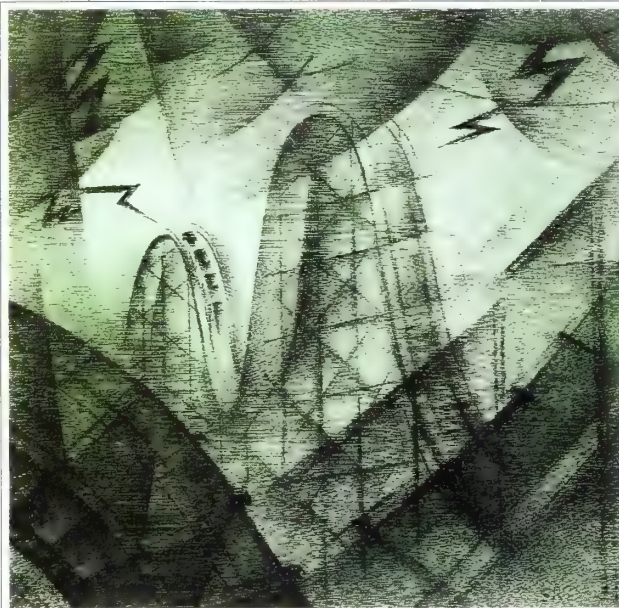
Forecasting a double dip is not as farfetched as it may seem. In each of the past four recessions, GNP posted a positive quarter only to resume falling. The temporary bounce comes from an inventory rebound. "We get a double dip because of an inventory correction in the middle of a recession that then continues," says David M. Jones, chief economist at securities firm Aubrey G. Lanston & Co. The downturn keeps going, Jones argues, "because this is a balance-sheet recession caused by an overleveraged economy." With existing debt loads heavy and new credit hard to get, consumers and businesses can't increase spending.

Charles Lieberman, a managing director at Manufacturers Hanover Securities Corp., is unconvinced that even inventory rebuilding will give the economy much strength. He suspects that much of the inventory drop has been in gasoline and other fuels. That's why crude-oil imports have fallen. Adds Lieberman: "At some point, we'll have to replenish these inventories. But we won't get a bump up from inventory accumulation because it will be matched by an increase in oil imports," which will subtract from GNP growth.

Even with a rise in inventories, bears argue that the fundamentals in the economy are too shaky to support a

recovery. Lieberman calculates that growth prospects in each sector are so weak that they don't add up to an expanding economy overall.

According to double-dippers, the negatives include banking-sector troubles, high long-term interest rates, an oversupply of office and retail space, and the overhang of debt on the books of



Double dip

In the past four recessions, real GNP posted a positive quarter only to plunge again. The possible culprit this time: Too much debt

consumers and businesses. And state and local governments, instead of boosting their local economies with tax cuts or spending programs, must balance their budgets and are devising new ways to pick taxpayers' pockets.

Adding to the woes, say the bears, is the federal deficit, which prevents Washington from stimulating the economy. And the Federal Reserve Board's reluctance to let short-term interest rates fall further will also prolong the downturn, warn some economists.

The momentum of a rebounding economy might surmount one or two of these drags, these forecasters agree. But because the negatives are so large and affect nearly all sectors, they will derail any nascent uptick in overall economic activity.

Take consumer spending, the most important segment of the economy

Both retail-sales and consumer-spending data have been upbeat in recent months. But households lack the cash to keep up the faster buying pace. Real disposable income has taken one of its worst slides in history. Savings are almost nonexistent, and debt levels remain onerously high.

'OLD BILLS.' David A. Levy, who heads his own forecasting firm in Chappaqua, N.Y., argues that even when incomes stabilize, the money "will go to pay off old bills and replenish bank accounts." He says consumers will increase buying of necessities such as food, not big-ticket items such as new cars.

The rise in long-term interest rates are another reason to hold off on the bubbly, warns

the doom-and-gloom contingent. Housing, in particular, is vulnerable. "Even if housing recovers," says Lieberman, "it's mathematically impossible for the industry to provide much thrust to the economy" because fewer new households are being formed in the 1990s than in the previous two decades. Lieberman figures that even if a third of home-construction firms closed, the rest of the industry could build all of the new homes needed.

By autumn, these double-dippers may well look like fools. But for now, they're sticking to their guns and refusing to join the recovery party. Any effervescence in the economy, they maintain, will soon fizzle out.

By Kathleen Madigan in New York

Where do you want to be in 10 years?



When the sun comes up, exactly 3,653 mornings from this one, where will you be?

Working full-time? Part-time? Working for yourself? Not working at all?

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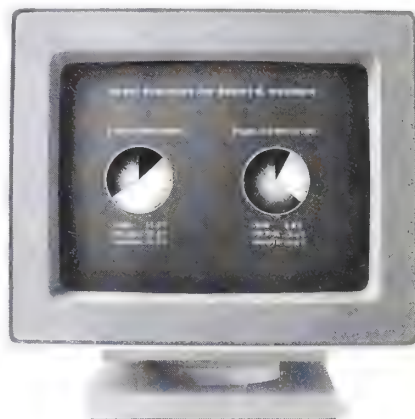
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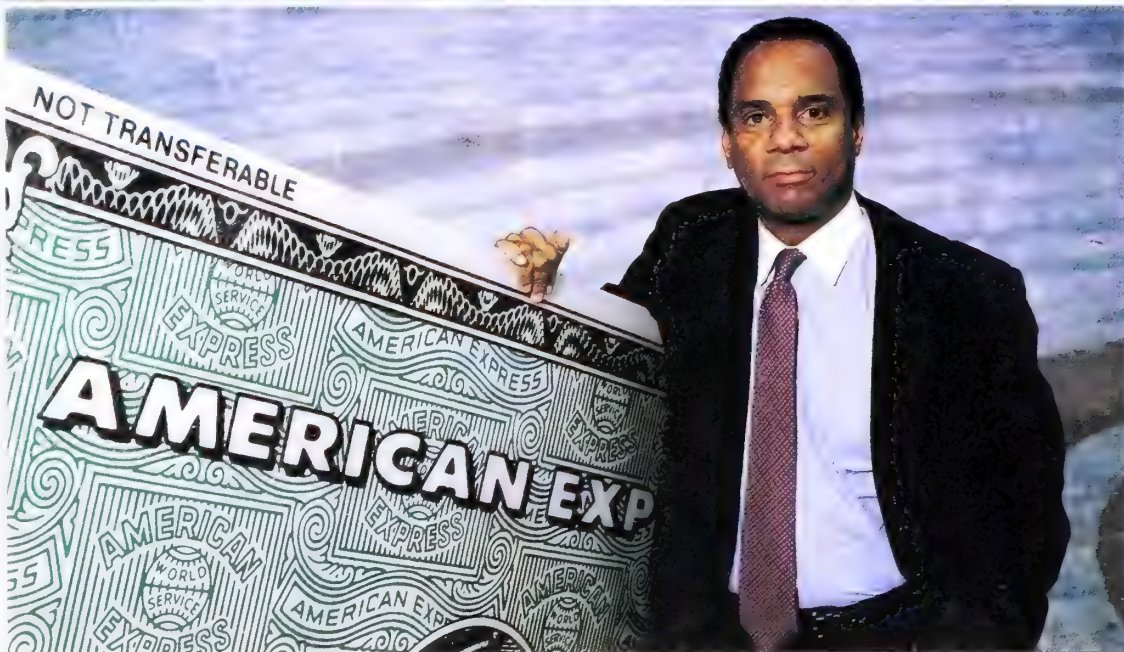
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'We have not suffered any harm. We are signing up thousands of restaurants and other establishments'

KENNETH I. CHENAULT
American Express

AMEX FIGHTS TO DISCOURAGE DEFECTORS

It's moving fast to mollify merchants, negotiating card fees and offering marketing support

In mid-April, executives at U-Haul International Inc., the Reno (Nev.) vehicle rental company, read about a group of Boston restaurants that staged a modern-day version of the Boston Tea Party. The eateries threatened to boycott American Express Co. cards and complained that the merchant fees it collects every time a diner charges a meal were too high. AmEx responded by shaving off half a percentage point from its 3.25% fee to larger restaurants that file their charge records electronically.

Three weeks later, Gary Horton, U-Haul's chief financial officer, fired off a letter to Edwin M. Cooperman, co-CEO of AmEx's Travel Related Services Div., demanding a similar reduction. Why should U-Haul, which rang up \$88 million a year in AmEx charges, pay a higher fee than restaurants with only \$10 million a year in AmEx charges? If U-Haul got the same break, it would save about half a million a year in fees. U-Haul and AmEx are scheduled to discuss the issue in a few weeks.

Meanwhile, U-Haul is exploring whether to drop AmEx altogether. Like

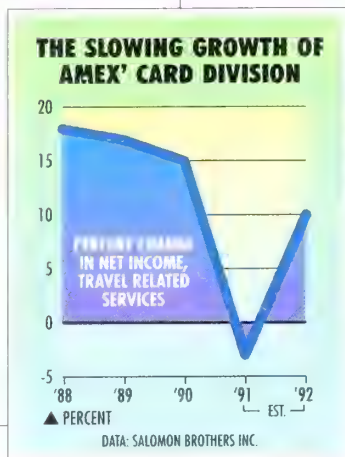
most merchants, U-Haul pays about one percentage point more if a customer uses an AmEx card rather than a Visa, Discover, or MasterCard. U-Haul is currently talking to other card issuers about whether more patronage from their cardholders would make up for the loss of AmEx's. Says U-Haul treasury analyst Tom Standish: "Will we lose business if we don't take the card? It's a guessing game."

Although the widely publicized merchant uprising against AmEx was initially confined to restaurants, it now appears to be spreading to other merchants, including direct-mail companies and retailers. AmEx denies a merchant backlash exists and downplays competitive pressures. "We have not suffered any harm," says Kenneth I. Chenault, president of AmEx's U.S. consumer card group. "We are

signing up thousands of restaurants and other establishments."

So far, the companies that supply the biggest portion of AmEx's business have been quiet. Airlines, which contribute about 25% of AmEx's merchant fees and hotels, contributing an additional 20%, don't appear to be among the protestors. Many have already negotiated lower fees. On June 13, AmEx cemented its relationship with airlines by announcing its Membership Miles program, which lets cardholders earn frequent-flyer mileage on seven carriers. It should also boost charge volume and merchant loyalty.

Yet AmEx is also losing some commercial customers. One Boston restaurant, Biba, owned by Lydia Shire, dropped the AmEx card in April, according to its assistant manager, who suffered no loss of business. A much larger de-



tor is Carnival Cruise Lines Inc., which had been a preferred supplier of cruises through AmEx-owned travel agencies since 1983. In September, 1989, says Robert H. Dickinson, the Miami-based line's senior vice-president for sales and marketing, Carnival began negotiating with AmEx to reduce its fees from more than 3% to something in line with the 1.5% they were paying Visa. After seven months of talks, AmEx made an offer that "went from highly exorbitant to exorbitant," says Dickinson. Carnival declined.

CHURCH BURNING. Midway through the talks the company decided to stop using the AmEx card. Since then, Carnival's business has grown 30%, and the amount charged on Visa and MasterCard has increased 15%, says Dickinson. "It tells me that AmEx's theory—that Visa and MasterCard are a necessary ingredient for travel and entertainment card purchases—is totally debunked by our experience," Dickinson says. "Ninety-nine percent of our AmEx cardholders have either Visa or MasterCard." Says Lawrence T. Kurlander, an AmEx spokesman: "We decided to move upscale with Royal Caribbean [a preferred provider], and they [Carnival] decided to go downscale with Visa."

According to Dickinson, AmEx retaliated by showing a slide of a burning



Part of the Boston boycott, Shire's restaurant no longer accepts the AmEx card. And business hasn't dropped a bit

LYDIA SHIRE
Biba

eroded less than a percent over the past five years. Yet the growth of Travel Related Service profits—two-thirds of which come from the card—has slowed considerably more (chart). "It's still a wonderful franchise," says John Keefe, an analyst at Lipper Analytical Securities. "But some of the excessive profits are gone, and growth will be slower."

American Express is aggressively seeking to seize the initiative. In coming months, says AmEx's Chenault, the company will announce "major strategic initiatives" which he declined to de-

said it no longer accepted the AmEx card. Within weeks, AmEx cut a deal with Steven Wishner, treasurer of Maxx owner TJX Cos., with annual sales of \$2.5 billion. Wishner declines to discuss details. The Chicago store has taken down its sign. And just two days after Marshall's, a large Rye (N.Y.)-based discount retailer, tried dropping the card, an AmEx team flew in for a visit. AmEx didn't lower its fee but "agreed to give Marshall's access to its customer data base and to share in marketing support," says a Marshall's spokesman.

Squeezed by higher U.S. postal and United Parcel Service Inc. rates, direct mail retailers such as Lands' End Inc., a \$604 million business in Dodgeville, Wis., are also trying to negotiate concessions. Most disavow any interest in boycotts. "We're not joining the Boston Tea Party," says Paul T. Soulier, controller at San Francisco-based Williams-Sonoma Inc., a cataloguer. "They need us, and we need them." Yet \$35 million Fort Lauderdale (Fla.)-based Joan Cook Inc. is testing half its Postscripts catalog distribution without AmEx as a choice. "Why should we pay double [Visa's and MasterCard's] rates when everybody has so many other choices?" says Harold L. Schwartz, the company's CEO.

VISA TIP TRAYS. AmEx's competitors are trying to capitalize on and inflame the merchant discontent. Discover sent a team to Boston this spring that signed up 300 new restaurants, boosting its local penetration from 23% to 78%. AmEx "is a dike with an awful lot of holes in it," says Michael Levitt, senior vice-president of Discover Services Inc.'s merchant sales.

Visa, which had no salespeople wooing merchants 18 months ago, now has six. Visa confirms that it is paying the lawyers' fees for the Boston restaurateurs. Last August, it launched a marketing blitz to convince merchants that Visa is better for them than AmEx. The centerpiece of the campaign is a "profit im-

AmEx theory—
that it is
necessary for
Visa & MasterCard
card
purchases—'was
totally debunked
by our experience'

BOB DICKINSON
Carnival Cruise Lines



Carnival brochure at a convention of AmEx-owned travel agencies earlier this year in San Diego. The idea was to discourage any bookings on Carnival cruises. "I regret to say that I can't deny it," says an AmEx spokesman. Dickinson's comment: "They give new meaning to the word arrogance."

Whatever the impact on American Express of the merchant uprising, there is no question that AmEx is suffering from white-hot competition in the credit-card business. AmEx's market share, at 24% of all U.S. charge volume, has

scribe. AmEx's overall strategy is to stress to merchants its upscale cardholders, who charge an average of \$3,409 a year vs. Visa's \$1,122 per card. "American Express is a single company with one of the strongest brand names in the American consumer market," says Chenault. "The AmEx decal says something about the establishment."

AmEx is moving swiftly to mollify disaffected merchants, especially retailers. In April, T.J. Maxx, a big discount retailer based in Framingham, Mass., displayed a sign in a Chicago store that

provement calculator," which lets merchants figure out their savings if customers use Visa instead of AmEx. The card giant responded with ads saying that Visa was about to hike its own rates.

Visa is also encouraging merchants to jettison their AmEx signs, card-printing devices, and tip trays, and replace them with Visa versions. "We're like the boy pointing out that the emperor has no clothes," says Brad Morgan, executive vice-president of marketing and sales at Visa. "It was a company close to

getting monopoly pricing based on a myth. We've been exposing the myth."

It's unclear what all of this will cost AmEx. Sanford C. Bernstein & Co. estimates that concessions given to restaurants will cost AmEx \$30 million a year. But the bigger worry on Wall Street is how much longer AmEx can retain its enviable record of profitability. The 18% growth rate of Travel Related Services in the 1980s will decline to 10% in 1992, according to Salomon Brothers Inc. And some AmEx stockholders are restless. One of the largest, Fidelity Management

& Research Co., has reduced its position substantially, say Street sources.

"The card business is the heart and soul of American Express," says Dean Witter Reynolds Inc. analyst Michael Lewis. "Just how much does the competition hurt it?" Right now, perhaps not much. But keeping dissatisfied merchants happy and competitors at bay will test AmEx's awesome marketing muscle as it's never been tested before.

By Leah Nathans Spiro in New York with Geoffrey Smith in Boston and Marc Shao in San Francisco

RUMBLINGS OF A PLASTIC RATE WAR

The credit-card wars seem to reach new levels of bellicosity almost daily. On June 17, yet another company, Ford Motor Co., announced that it will introduce its own credit card into the fray. The battle thus far has been waged mainly over considerations such as annual fees and special enhancements. The one key feature the combatants haven't tussled over: interest rates on unpaid balances, which remain at 19.8% for most major issuers.

Now, that's changing. "We may be seeing the rumblings of a rate war," says Robert B. McKinley, publisher of RAM Research's *Bankcard Update*. And the impact on card issuers, especially banks, could be chilling. "The most profitable part of lending is credit cards," says Thomas H. Hanley, a bank analyst at Salomon Brothers Inc. "Chipping away at credit-card margins is the last thing the industry needs right now."

Until recently, the conventional wisdom was that cardholders are insensitive to the interest rates they pay because they expect to pay balances promptly. But today, only 32% of cardholders do so, vs. over 50% a decade ago. The average balance, \$1,626, is double that of a decade ago.

NOW'S THE TIME. One of the first salvos in the growing rate war was launched in May, in ads for American Express Co.'s variable-rate Optima card. Full-page ads asked consumers: "Why pay VISA or MasterCard over 19.00% a year? When you have a smarter option at 16.25%." Optima, which charges a rate equal to the prime rate plus 6.75%, was capitalizing on a drop in the prime. "With costs of funds lower, now is a good time for people who want market share to use rate as a promotion," says Kenneth R. Keck, chairman of the bank-card division of the American Bankers Assn.

Lesser-ranked issuers followed suit. National Westminster Bank USA, 50th by market share, has been running comparison ads asking: "Why pay 18.9% or 17.8% interest when the interest rate on a NatWest Visa Gold Card

It's Clearly In Your Interest To Get A Visa Gold Card From Us.

No Annual Fee For The First Year

NatWest	15.0% ^{APR}
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"The increase in applications is so high that it's incredible," says a NatWest exec

is just 15.0%?" And 25th-ranked Wachovia Bank Card Services, a subsidiary of Atlanta-based Wachovia Corp., is hawking its new variable-rate card, which tacks 2.9% onto the prime to offer an 11.4 rate. "We're up against

formidable competitors with deep pockets," says Ray S. Costner, Wachovia's senior vice-president for credit-card marketing. "You've got to decide where you're going to draw your line in the dirt and say, 'This is the ground we want to play on.' We want to be with the low rate."

Some issuers are trying to recoup lost interest revenues by hiking annual fees. NatWest's fee on its 15% gold card is \$40, though the first year's fee is waived for new customers. "The increase in applications is so high that it's incredible," says Joseph A. Pisano, the bank's vice-president for consumer credit.

NO PROBLEM. Critics of low-rate cards warn that they attract customers who are higher credit risks, but many in the industry say that's no longer true. "Based on our experience with our existing 14.98% card, we expect the new card to interest people who handle their credit without frequent problems," says Wachovia's Costner.

Experts don't expect interest-rate skirmishes to escalate into all-out hostilities overnight. "There isn't going to be any mass lowering of rates," says Spencer Nilson, publisher of *Nilson Report*, which tracks the credit-card market. But many others expect the trend to intensify as issuers that offer low rates begin to steal share from market leaders. "I think it's inevitable—even this year—that one of the top seven issuers will cut rates," says McKinley of *Bankcard Update*. "Once somebody starts to crack, no one will want to be left out." Least of all, consumers.

By Suzanne Woolley in New York

THE NOOSE THAT'S CHOKING THE NIKKEI

The Bank of Japan's relentless tight-money policy shows no signs of easing up

Masahiko Tsuyuzaki, chief trader for Tokyo's Tachibana Securities, is in a foul mood. The economy grew at close to an 11.2% annual rate in the first quarter, but the stock market is going nowhere. The problem is high interest rates, and the market's quandary is that the stronger the economy, the less likely it is that rates will come down. "Making money is like trying to walk up a down escalator," sighs the trader. "We're desperate."

So is most of the Japanese stock market. The U.S. and European markets are up about 15% and 21%, respectively, this year, but the Nikkei average is barely ahead at all. The Nikkei, which plunged 39% last year, had staged a comeback, to 27,147, in mid-March. But the rally could not be sustained, and in recent weeks, the market has deteriorated. On June 19, the Nikkei plunged nearly 700 points, or 2.8%. Shares in such big Japanese companies as Hitachi, Matsushita, NEC, and Sony are at or near 52-week lows.

The situation isn't likely to improve much. With Japanese certificates of deposit yielding a lofty 7.8%, the engines of the Japanese stock market—big life insurance companies and cash-rich corporations—have no reason to load up on stocks. Traders say the heavy-weight investors probably won't show up again until money-market yields drop to 6%. And no one sees that happening anytime soon. As a result, the Nikkei could hover around its current 24,000 level for months to come.

MONEY DAYS. What's bedeviling the market is Bank of Japan Governor Yasushi Mieno's anti-inflationary tight-money policy, which he has pursued unrelentingly for nearly two years. Inflation in Japan is running at a 3.5% annualized rate and falling. That's mild by U.S. standards. But Mieno thinks it's too high and is determined to stamp it out.

Mieno is especially anxious to keep at

bay the speculators who ran up land prices—and eventually stock prices—to artificially high levels during the easy money days of the late 1980s. Even though real estate prices have fallen 15%, and near 30% for Tokyo condominiums, they have further to go before the central bank will let up. "We don't want land prices to come up again," says a Bank of Japan economist. "This is crucial for us."

For a while, some market participants felt that the central bank would ease up a bit by early summer. But the dollar's surge against the yen, as the foreign-exchange markets anticipate an economic recovery in the U.S., has obliterated any hope of that. Mieno won't dare undercut an already weakened yen by fur-

Fund, for instance, has about 40% of its \$360 million portfolio in small-company stocks, chiefly domestic service companies such as Nippon Systems Development, a software house, and Aoyama Trading, a men's clothing chain. Small stocks' rise has been fueled mainly by individual speculators. But with some OTC shares now sporting price-earnings ratios of 90, this sector, too, could soon run out of steam.

Most foreign investors, though, are aggressively bargain-hunting Tokyo blue chips. Elizabeth X. G. Tran, managing director of Prudential Asia Fund Management Ltd., likes Canon and auto parts makers such as Nippondenso and Daiki Aluminum. And because exports are on the rise again (page 40), Marshall

Auerback, portfolio manager of the \$70 million GT Japan Growth Fund, has placed 40% of his fund in such well-recognized names as Kyocera, Sharp, Sony, and Toyota.

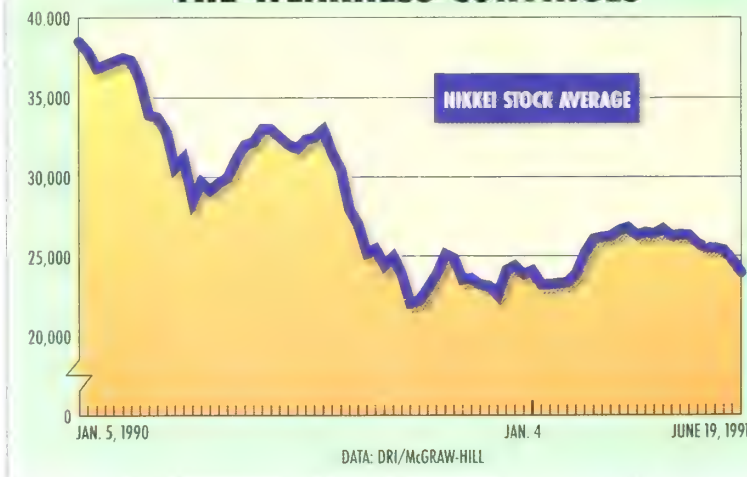
If foreigners keep buying, 1991 will likely be the first year in the last seven that foreign investors made net purchases of Japanese stocks. In the February-March runup, foreigners bought about \$1 billion net. In May, foreign brokerage firms led by Salomon Brothers Inc. and Morgan Stanley & Co., captured a hefty 13% of trading

volume. Salomon and Morgan also dominate the stock-index futures market.

But foreigners don't have enough firepower to turn the massive Tokyo market around, especially when the Japanese are dumping stock on any sign of strength. Takashi Yamaguchi, fund manager for Seiyu Investment Management, for example, has cut his equity holdings to 30%, from about 90% several months ago. As long as interest rates stay high, Yamaguchi will have lots of company.

By Karen Lowry Miller in Tokyo, with William Glasgall and Jeffrey M. Laderman in New York

JAPANESE STOCKS: THE WEAKNESS CONTINUES



ther lowering interest rates. The best the markets can hope for, predicts Tet-suo Tsukimura, an economist at Smith Barney International in Tokyo, is that monetary policy "will move from tight to less tight."

While the big Japanese investors are content to keep their money in the bank, foreign investors have shown some willingness to bet that Tokyo might follow other markets upward.

Some foreign investors have been looking for gains in secondary stocks traded on the Tokyo Stock Exchange, up 21% this year, or on the over-the-counter market, up 48%. The U.S.-based Japan

BY GENE G. MARCIAL

MAXUS ENERGY'S GLOBAL POCKETS OF STRENGTH

Maxus Energy, which has been floating in red ink since 1986, finally turned profitable in the first quarter of this year, and some analysts think the oil-and-gas producer will be in the black for all of 1991. But the Street is down on energy stocks and hasn't paid much attention. So Maxus Energy has meandered between 7 and 9 since January. But that's just fine for big investors who scout for undervalued energy producers. Those pros figure that with Maxus' huge overseas assets, its shares could double in the next 6 to 12 months. The stock was as high as 16 in 1987.

But that's not all that's attracting some smart money to Maxus (formerly known as Diamond Shamrock). Whispers are that Atlantic Richfield, which operates one of Maxus' Indonesian properties, has its eye on the company. ARCO informally approached some Maxus bigwigs recently about the possibility of a buyout," says one New York money manager. He thinks Maxus Chairman and CEO Charles Blackburn, who's 63, wouldn't be averse to selling at the right price. And he says if Maxus entertains an offer, such majors as Mobil and Spain's state-owned oil company, Repsol, are likely to be interested in making a bid. (A Maxus spokeswoman says ARCO hasn't approached Maxus.)

CZECH MATE. Dallas-based Maxus owns large oil-and-gas properties in Southeast Sumatra and in Colombia, where it made a big natural-gas discovery in June. The company has also been aggressively signing exploration deals in Paraguay, Bulgaria, and Czechoslovakia. Net operating cash from international operations jumped nearly 57% in the first quarter, largely because of Sumatran production. And analysts expect that with its Indonesian fields now on stream, Maxus' worldwide net oil production will jump about 50% in 1991. Maxus spun off its refining-and-marketing operations in 1987—when it was still known as Diamond Shamrock—after T. Boone Pickens Jr. took steps to raid the company.

Alan Gaines, president of securities firm Gaines Berland, agrees that at its current price, Maxus is way undervalued. He figures the company is selling

MAXUS ENERGY: STILL ON A JAGGED COURSE



DATA: BRIDGE INFORMATION SYSTEMS INC.

at only about three times its cash flow of \$3 a share. Gaines thinks Maxus is worth at least five times its cash flow. With North America already "over-explored for oil," says Gaines, demand for overseas properties will eventually jump—and "Maxus has a lot of such properties." The company had net proved reserves of 171 million barrels of oil and 663 billion cubic feet of gas at yearend 1990, and it's also drilling in the Gulf of Mexico. Gaines notes that some executives of Maxus believe the company is worth \$15 to \$20 a share.

LOTS OF WAYS TO WIN WITH CAROLCO

The stock of Live Entertainment jumped a couple of points, to 13, on June 10, the day Carolco Pictures proposed a "business combination" with Live. Nothing unusual. Far more intriguing, though, is that the shares of Carolco, which already owns 47% of Live, didn't tumble—they've been edging up, to \$8 a share.

Why? Some pros think Carolco is itself a buyout candidate. And the acquisition of Live would make Carolco "a top-notch Hollywood movie and home-video company," says Paul Wick, a portfolio manager at J. & W. Seligman.

Wick thinks the Street hasn't recognized the values in Carolco, which finances, produces, and leases motion pictures to theaters worldwide, including the pay-TV and home-video markets. Its latest releases include *Terminator II*, and a movie with Michael Douglas called *Basic Instincts* will be released later this year. Live, a major distributor of prerecorded music as

well as videocassettes, would give Carolco a much larger share of the home-video business, plus Live's huge and valuable children's video library.

A shareholder lawsuit filed recently seeks to block Carolco's proposed acquisition of Live. But that hasn't discouraged suitors of Carolco. One big investor says that with Live in Carolco's pocket, Chairman and CEO Mario Kassir, who has a controlling 57% stake, will either take Carolco private or sell it to one of its major shareholders. One is Japan's Pioneer Electronic, which owns a 10% stake. The others: France's Canal Plus Productions, 5%; the Fiat Group, 3%; and a British group, 3%. Wick says buying Carolco shares "is a win-win situation."

A FULL DANCE CARD FOR INTERFACE?

Interface Chairman and CEO Ray Anderson insists that his shareholders will find 1991 highly rewarding. So far, the stock has been rising, to 13 from 8½ in January. But Interface, the world's largest maker of carpet-tile used mainly in offices, traded as high as 20 last year. Profits were down last year, and since they have continued to limp, 1991 earnings are likely to be down again. So what's the deal?

Anderson isn't saying just yet. But here's what one pro says: When he was in Europe in May, Anderson may have held preparatory talks with executives of a large European fabric company about a merger or strategic alliance. "Something is definitely going on," says this pro.

And that's not all. Another big investor says carpet maker Shaw Industries is interested in acquiring Interface. Shaw President Bob Shaw "would write the check right now if Anderson agreed," he says. Shaw has a small carpet-tile division, but Bob Shaw is said to be unhappy about its progress.

Binkley Short, who runs the OTC Fund, says Shaw Industries would aggressively market carpet-tiles, thereby upping demand. In this growth market, says Short, "there's plenty of room" for both Shaw and Interface.

Another thing Anderson may do is sell Interface's Guilford Industries, which makes fabrics for panels, seating furniture, walls, and window draperies. Its earnings nosedived in the second quarter because of the slump in housing construction. If Guilford were sold, the money could go toward cutting Interface's debt of \$260 million.

LIQUOR



ON DISPLAY AT ODDBINS: TO DISTILLERS, BRITAIN IS A VAST, UNTAPPED MARKET

SWEET SALES FOR SOUR MASH—ABROAD

Bourbon is flowing in Japan, Australia, and other affluent countries

Rebel Yell. To U.S. drinkers, the catchy name of this bourbon evokes the Old South and the war cry of the Confederacy.

The brand is popular in Australia, too, but consumers there associate its name with rebels of the rock 'n' roll variety. In ads that are heavy on electric-guitar music, distributor United Distillers PLC shows an ultracool dude in a black leather jacket. The product's slogan is "Give us a yell"—the Australian way of saying: "Call me when you want me." And Rebel Yell is backed by a three-year, \$6 million ad campaign.

LEATHER & METAL. Rebel Yell's campaign is just one of dozens the bourbon industry is waging around the world. "Export is the hot spot," says Barry M. Berish, president of Jim Beam Brands Co., the No. 1 distiller. From 1985 to 1990, total exports of Kentucky bourbon and its close cousin, Tennessee whiskey, more than tripled, to an estimated 11 million 100-proof gallons. Recession and higher taxes worldwide have hurt overall growth, but distillers are optimistic. After scoring big in Japan, sour-mash makers are busily advertising in Australia, Britain, and other affluent markets. And top brands, such

as Jack Daniel's, are showing blistering foreign growth of 25% a year and up.

The outlook abroad is better than in the U.S., where "the whole product category has been very mature," says Anthony Greener, managing director of Guinness PLC's United Distillers, which owns Rebel Yell and other brands. Rising temperance and the vodka fad have also hurt. M. Shanken Communications, which publishes liquor-sales data, estimates that U.S. bourbon sales slid from more than 30 million cases in 1975 to about 17 million recently.

For many years, bourbon suffered from a lowbrow reputation overseas. "Americans were the fellows in plaid

trousers waving big, fat cigars," explains Brian O'Byrne, international vice president at Austin Nichols Distilling, makers of Wild Turkey. The whiskey these uncouth types drank obviously lacked class. But the surging popularity of American pop culture has changed that. "Now, anything that hooks in American heritage does well abroad," says Bill Samuels Jr., who heads Maker's Mark Distillery Inc., which expects to export about 21,000 cases of its prestige bourbon this year.

STEPPING OUT. In Japan, distillers have exploited that American heritage quite nicely. I. W. Harper's distributors have focused on the bourbon's label, which features a dandy in a top hat. For young, affluent Japanese, the Harper "Bowling Man" embodies Manhattan sophistication as he cavorts in Japanese ads on New York rooftops. The Japanese drink more of United Distiller I. W. Harper than White Horse, the leading Scotch in Japan.

Despite continued success, bourbon growth in Japan slackened in 1990, from 50% a year to the low teens. So distillers are turning to other markets. In Australia, Rebel Yell, Old Crow, and Wild Turkey have joined Jim Beam, which has been there since 1960 and sells more than a half-million cases a year with a cowboy-image ads. Wild Turkey's recent campaign features American bartenders discussing the brand's virtues.

Bourbon makers also see an untapped market in much of Europe. Britain, for example, bought only 100,000 cases in 1989, but trendsetting liquor chains there, such as Oddbins, have started stocking George Dickel and other bourbons. Of course, not everyone is calling for shots. Says James Bruxner, chairman of Justerini & Brooks, maker of J & S Scotch: "To a Scotch drinker like me, bourbon has a very nasty taste." But he concedes that young British consumers find drinking bourbon "a bit daring."

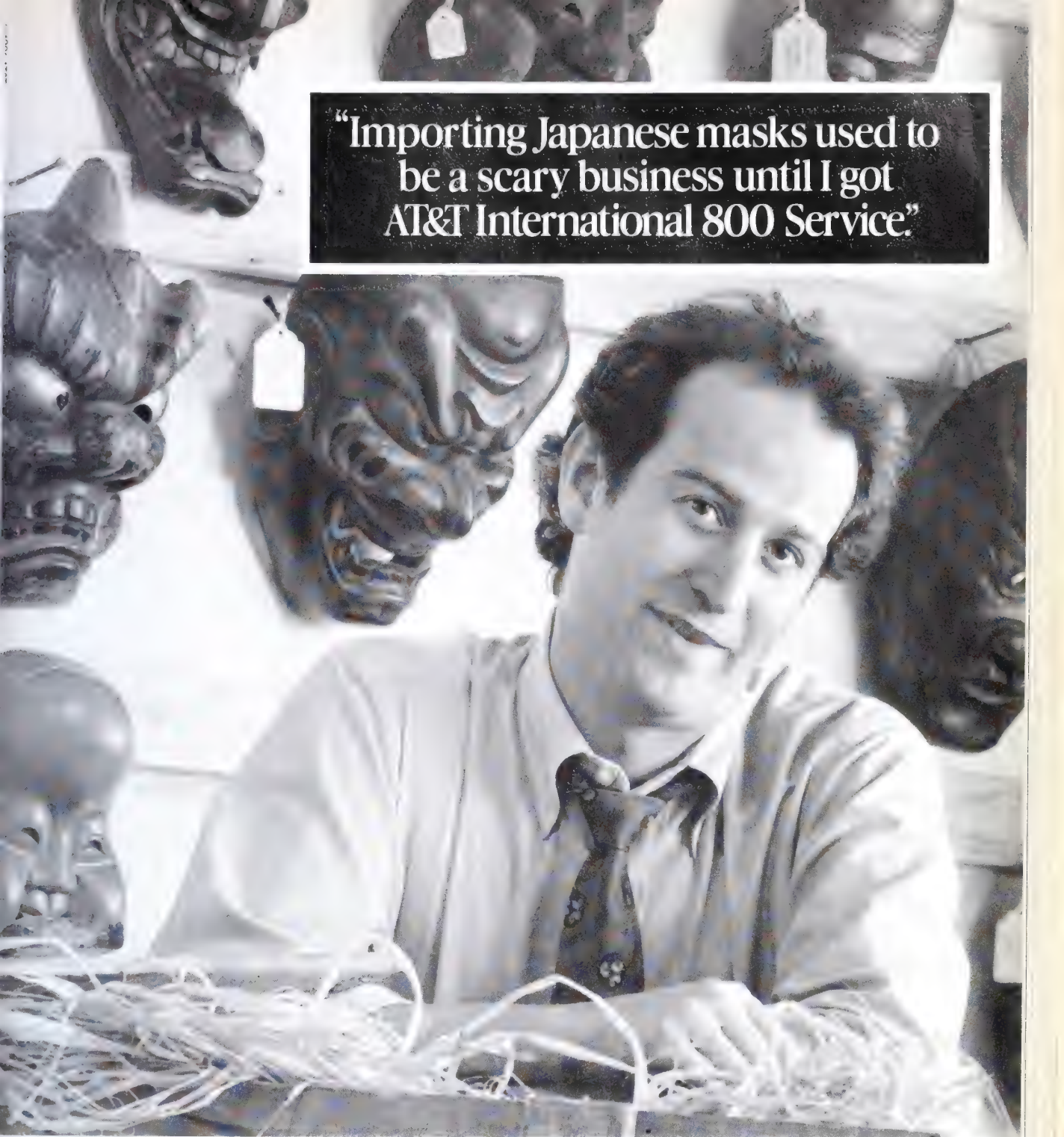
Europe may not be the roaring success Japan has been. Despite good results in Italy, Emanuele Bassino, managing director of importer Spirit, doesn't foresee a bourbon boom there. "It's a trend among young professionals who have traveled abroad," he says. "But it's a contained trend among a certain set."

Don't bother telling distillers that. The industry is betting that bourbon will catch on big in Greece and Spain. And to capitalize on foreign sales, United Distillers is investing \$20 million to expand production in Kentucky. The Old South won't rise again, but bourbon makers think they have a fighting chance.

By Christopher Power in New York, with Robert Neff in Tokyo and bureau reports

BOURBON STREAK





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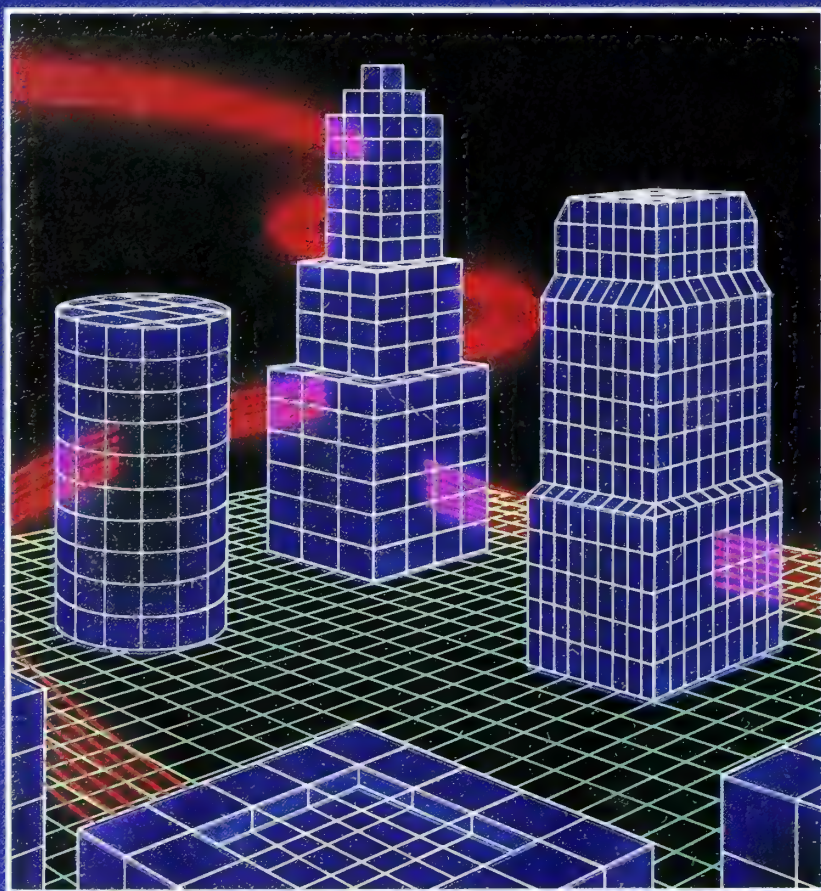
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BusinessWeek

ED BY PETER FINCH

ORIT GADIESH: FROM ISRAEL'S ARMY TO THE CONSULTING TRENCHES



At Harvard business school, she was "Machine Gun Orit"—intense, talkative, and aggressive. The rumor was, Orit Gadish had commanded tanks in the Israeli army. Actually, she served on the personal staff of the head of the operations branch of the Israel Defense Forces.

These days, nearly 15 years later, Gadish is getting battlefield experience as managing director of the Boston office of management consultant Bain & Co. For the past year, Bain has struggled with slowing growth and enormous bank debt. On June 14, it reached a deal to wipe out much of

debt and transfer majority ownership to a new group of 75 executives, including Gadish.

Gadish, in her early 40s but unwilling to give her exact age, helped arrange the tough restructuring. Now, she'll run Bain's largest office, with 220 consultants. "We went through a tricky period," she says. But after a time of healing, some measure of optimism has returned to Bain, employees say. A graduate of Hebrew University of Jerusalem, Gadish is a top marketing student at Harvard B-school. At Bain, she quickly established a reputation for deft analysis—and toughness. Returning from her first client presentation, she was hit in the face by a steel pole that crashed through her office window. She was rushed to a hospital for minor surgery, then joined a client for dinner. "I've had interesting offers to do other things," including returning to Harvard as a faculty member, she says. But she has stayed with consulting. As she puts it: "I get a high from it."

By Keith H. Hammonds in Boston

ELLA WILLIAMS: A COLLEGE DROPOUT WITH THE RIGHT STUFF

S gutsy decisions seem to come naturally for Ella D. Williams. After 13 years on the accounting staff at Hughes Aircraft Co., Williams quit to get a college degree. But her 1981 divorce forced her to drop out of the University of California at Los Angeles to support her two children. Unfazed, she made another bold move. She started her own engineering consulting firm, Aegir Systems Inc.

It was quite a leap. But, says Williams: "I knew what Hughes did—they wrote proposals and management plans. So that's the big deal? I figured I could do that and hire the engineers" later. She took out a \$65,000 second mortgage and started writing proposals, buttering up top prospects with homemade treats from her kitchen. Her first contract, three years in the making, was an \$8 million award from the Pacific Missile Test Center to provide software and engineering ser-

vices. To support her family, she worked as a temporary secretary.

Today, Aegir, based in Camarillo, Calif., has 60 full-time employees and brings in around \$4 million a year. In the past year, Aegir has opened branches in Los Angeles and Washington, D.C., to focus on transportation consulting. So far, Aegir has won more than \$1 million in transportation-related contracts, including a study of the debit-card plan for the Los Angeles subway system.

Later this year, Williams plans to start another venture, a nonprofit cheesecake "factory." The idea is to teach skills to disadvantaged youths and use the proceeds for scholarships. As anyone who has tried one of her cheesecakes can attest, you don't need a consultant to know they're well-engineered.

By Larry Armstrong in Camarillo, Calif.



KENNETH COLE: DOING THE OLD SOFT-SHOE TO SUCCESS



To get attention for his debut collection of footwear back in 1982, Kenneth Cole parked a 44-foot van on a busy Manhattan street corner and set up a giant display. He got a permit from the mayor's office under the pretense of filming a movie, *The Beginning of a Shoe Company*. He even hired a director. "Sometimes there

was film in the camera, sometimes there wasn't," he admits.

The movie never materialized, but the debut was a success. Cole, 37, now has shoe stores in New York, San Francisco, Atlanta, and Amsterdam. His lines of shoes and accessories are also featured in top department stores, such as Lord & Taylor and Saks Fifth Avenue, with prices ranging from \$75 to \$200. A funny continuing ad campaign has helped raise Cole's visibility. In one, a jet from now-defunct Eastern Air Lines Inc. was pictured with his shoes. The headline: "Some forms of transportation are more reliable than others."

Cole fully intended to go to law school after finishing Emory University in 1976. But he got such a kick out of designing shoes for his dad's Brooklyn shoe company he stuck with it, founding Kenneth Cole Productions Inc. in 1982. He says 1991 sales will top \$100 million, but he declines to disclose profits.

Today, the company licenses Cole's name for a number of accessories as well as Unlisted, a line of moderately priced shoes. Next for Cole, who married the daughter of New York Governor Mario M. Cuomo in 1987, is a line of children's shoes. And he recently signed a deal with Japan's Seibu department stores to sell all the Kenneth Cole lines. No, he's not going to replay the filmmaking caper for his Tokyo debut.

By Heather Keets in New York

PC SLUMP? WHAT PC SLUMP?

Things are humming at Dell Computer, thanks to R&D and service

Don't let Michael S. Dell hear you call his \$546 million personal-computer company a mail-order business. Sure, Dell Computer Corp. got its start selling PCs through the mail. And many customers still respond to print ads, dial an 800 number to order the machines, then await delivery by return mail—just like customers of the Franklin Mint. But the company's 26-year-old chairman prefers to emphasize Dell's research, manufacturing, service, and marketing smarts. Those, he says, set Dell apart from other companies that skirt computer stores to sell PCs directly to the public. Mostly, he wants his company to be known as a force to be reckoned with in the PC industry.

Lately, he has been getting his way. At a time when traditional computer retailing is disintegrating and, one reason why, top PC makers are having a dismal year, Dell's direct-sales approach makes it a standout. While Compaq Computer Corp., the leading maker of PC compatibles, expects a 15% decline in revenues in the June quarter, sales in Dell's first quarter, ended May 5, rose 45% to \$175 million. In the U.S. PC market, the company has hopped to No. 6, from No. 22 in 1989. And it ranked No. 1 in J.D. Power & Associates Inc.'s first-ever PC customer-satisfaction survey. Compaq now finds Dell such a competitive thorn that it has sued to stop it from running ads that compare its prices with Compaq's.

Dell launched his business at age 19 from a University of Texas dorm room. His strategy—selling IBM-compatible PCs through the mail to customers who were reluctant to pay computer-store prices—was an instant success. Now, Dell Computer is an international operation, employing 2,100 people and generating 35% of its sales overseas. Chairman Dell's stake is worth \$200 million.

GIANTS STUMBLE. From day one, Dell counted on low-cost direct marketing to undercut better-known brands that relied through the costly dealer system. "We call that the high-cost distribution strategy," says Joel J. Kocher, Dell's senior vice-president for U.S. sales and operations. Lately, it's also a high-risk strategy. Caught in a price war, computer store chains are undergoing a massive consolidation, and PC makers are watching dealer inventories pile up.

Dell has had its own shaky moments. Earnings took a hit in 1990, when Dell had an oversupply of memory chips and scrapped an ill-fated effort to build an engineering workstation. Profits plunged 65% for the year, to \$5 million. But in fiscal 1991, ended Feb. 3, the company bounced back, earning \$27 million. For the first quarter of this year, profits leapt nearly 50%. Analysts expect Dell

SO YOU WANNA BE A MAIL-ORDER STAR . . .

It doesn't take much to get into the mail-order personal-computer business. After all, Dell Computer Corp. founder Michael S. Dell did it from a college dorm. All you need is a supply of components such as disk drives, mother boards, and monitors—all available from dozens of suppliers. Then, you slap them together, run an advertisement in a computer magazine, and wait for the phones to ring.

Staying in business is another matter. Nearly 130 companies advertised computers for sale in the June, 1990, issue of *Computer Shopper*, the 800-plus-page PC mail-order bible. In this year's June issue, just half of those companies were still advertising.

JUST AS GOOD. But the survivors, companies such as Gateway 2000, CompuAdd, Northgate, and Zeos, are growing so fast they could soon give Dell a run for its mail-order money. The market is exploding, too. Mail-order companies will account for 29% of all PC sales in 1995, vs. 22% in 1991, figures market researcher WorkGroup Technologies Inc. That's be-

cause big business is discovering what consumers already know: Mail-order PCs are often as good as store brands, but they sell for up to 30% less.

The new buyers are people such as

Paul Q. Hannan, an engineer at General Motors Corp.'s automatic-transmission plant in Toledo. He has bought more than a dozen CompuAdd Corp. computers since 1989. The machines have been "rock-solid," Hannan says, and they were right. "We could buy two CompuAdd computers for the price of one IBM," he says.

To be sure, many customers are wary of buying a computer over the phone. Many mail-order PC suppliers offer trial periods of up to 60 days, money-back guarantees, long-term product warranties, and toll-free phone lines.

The best of the Dell "wannabes" are their role-model, design and build their own machines. Then they look for a way to market them to. Gateway 2000, for instance, claims it offers rock-bottom prices and focuses on pushing its own thing from assembling machines to answering phones, the North Sioux (S.D.) company sold more than 600 computers in 1990. Zeos International Ltd. in St. Paul, Minn., on the other hand, offers features that buyers get from other companies. Its computers, for instance, has two fans instead of one to extend the life of the PC's components. Northgate Computer Corp. emphasizes support. It recently helped build

DELL'S MAIL-ORDER RIVALS

Company/ Customers	1989 revenues Millions
COMPUADD GENERAL MOTORS, PRUDENTIAL	\$516*
GATEWAY 2000 AMOCO, TIME WARNER	\$275
NORTHGATE COMPUTER BRUNSWICK, LENDER'S BAGELS	\$203
ZEOS INTERNATIONAL SMITH CORONA, PFIZER	\$111

* Roughly half from its own stores



THE LINE: FROM ITS START IN A TEXAS DORM ROOM, DELL HAS GROWN TO 2,100 EMPLOYEES, WITH 40% OF ITS SALES OVERSEAS

ern \$43 million on sales of \$750 million fiscal 1992. Even after a \$100 million secondary stock offering in May, Dell's shares are up 38%, to 25, since Jan. 1. That record is particularly impressive given the state of the PC industry. Compaq isn't the only giant roiled by recession-inspired weak demand. IBM says low PC sales are one reason why second-quarter earnings will be 50% below

g-ball maker Brunswick Corp. re-engineered a mainframe computer system with a stack of 300 PCs.

ing costs in line, however, is the challenge faced by any mail-order retailer. Ask Northgate. After it added staff to call on big customers last year, overhead skyrocketed, and it lost \$10 million. Chairman Arthur B. Lazere, a new president, sacked the sales manager and refocused the Eden Prairie company on mail order. The payoff: Northgate reported a \$2.2 million profit last March quarter.

THE 'WALL.' Is there a limit to the number of PCs a mail-order company can sell? Bill Hayden, owner and chief executive officer of CompuAdd in Austin, thinks so: about \$250 million worth a year. At that point, he says, "everybody hits a wall," because there are so many mail-order suppliers and only so many PC buyers who are willing to shop by phone. That's why Dell branched out to direct sales and why Hayden added performance workstations and peripherals to his product line and opened a network of 93 stores.

Maybe somebody ought to tell Gateway about that wall: Chairman Theodore Levitt says he's going to sell \$500 million in PCs by mail this year.

By Lois Therrien in Chicago

what analysts had expected in March. And Apple Computer Inc. is planning its biggest layoff ever.

But the bad economy has been good for Dell—and for a few other companies that sell cutting-edge IBM PC clones cheap. Like Dell, AST Research Inc. sells PCs for 30% less than IBM and Compaq list prices. "Customers have less money to spend, but they're still looking for value and a quality product," says AST President Safi U. Qureshey. "Customers are judging us with their pocketbooks." Indeed, says Hilarius Fuchs, assistant vice-president for information systems at Continental Grain Co., "our traditional problem with Compaq has been pricing." For four years, Continental has purchased Dells to replace Compaqs.

Dell holds on to customers such as Continental through what Michael Dell calls "direct relationship marketing." In addition to cutting costs, the company's phone-sales strategy gives it direct input from customers—an important edge, he asserts, over competitors who rely on computer stores. Says Dell: "We take direct responsibility for the complete satisfaction of each and every customer."

SUPPORT. Calls are handled by hundreds of headset-wearing salespeople, who train for at least six months before hitting the phones in Dell's granite and glass Austin (Tex.) headquarters. The telemarketers work with buyers to customize orders, adding such options as a larger-capacity disk drive or a built-in modem. Then, specifications are sent via

computer network to a nearby plant. Finished PCs are shipped within five days.

Dell claims that 91% of customer problems are solved over the phone by his staff of 150 technicians. But the company also offers next-day, on-site service through a Xerox Corp. unit. "We get a great deal of attention from Dell's sales and support staff," says William Paquin,

vice-president for finance and systems at MCI International.

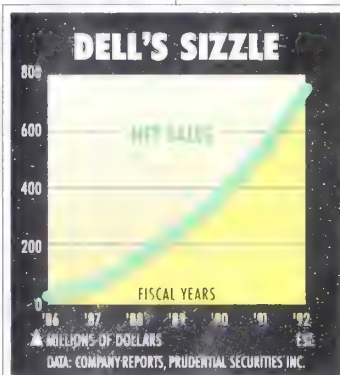
All this customer contact has helped Dell build a data base of 750,000 PC owners, who help it focus its marketing and pinpoint needed product improvements. It learned from its phone lines, for instance, that buyers wanted a Dell computer like Compaq's high-

powered Systempro.

Lately, Dell has moved beyond telephone sales. In 1988, it added a sales force to deal with large customers and signed up specialized sellers who customize Dell computers with their own software. In 1990, Dell even took a small step into retail, putting its PCs into Comp USA superstores.

Michael Dell's biggest worry now is that rivals, even big ones such as IBM, could ape his strategy. "I don't think for a second that our competitors are going to sit around and keep doing what they're doing, because it's clearly not working," he says. "I'm actually surprised that it's taken them so long to react." Maybe they were confused by the mail-order moniker.

By Stephanie Anderson Forest in Austin



BORLAND THE BARBARIAN

The software maker's marketing is 'uncivilized'—and it works

Philippe Kahn likes to think of himself as a barbarian. As chief executive of Borland International Inc., Kahn likes to use unconventional—and sometimes uncivilized—methods to avoid getting bogged down by corporate bureaucracy. When he has a big disagreement with another executive, they take a walk in the woods near Borland's Scotts Valley (Calif.) headquarters, where they can scream without being overheard. If people can't agree on a product feature, Kahn, 39, sometimes locks them in a room—all night, if necessary—until the issue is resolved. "We have lively meetings," says Kahn. "We throw things around."

Kahn's methods have helped

eight-year-old Borland conquer a surprising amount of territory. In recent years, he has turned it from a tiny seller of esoteric programming languages into a respected challenger to Lotus Development Corp. and Ashton-Tate Corp. Borland now controls about 20% of both the PC data-base and spreadsheet markets that those companies dominate (chart). As a result, in its fiscal year ended Mar. 31, Borland's revenues doubled, to \$226.8 million, and earnings jumped 127%, to \$11.8 million.

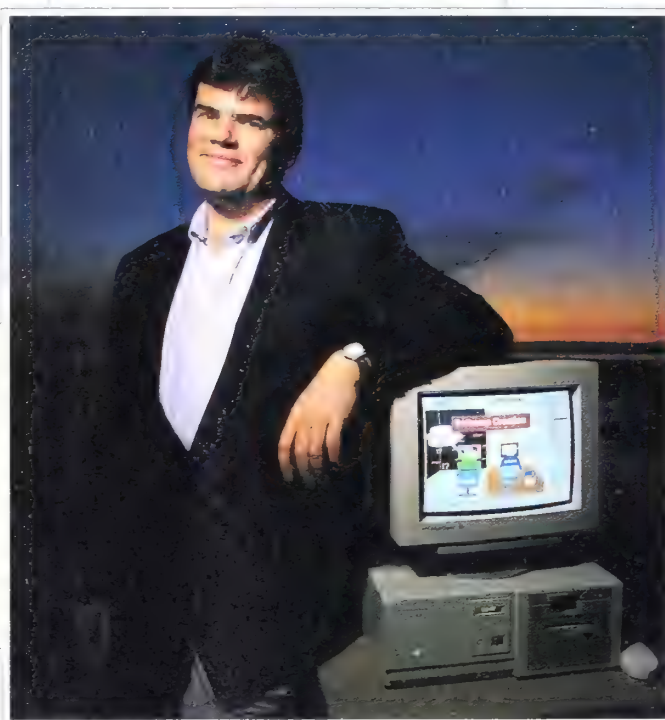
UNIQUE? Borland's recent momentum came from ruthlessly undercutting the industry's pricing structure. "Borland has changed normal PC software pricing," says Marshall L. Moseley, a Dataquest Inc. analyst. "Before, it was more of a gentleman's game." Kahn pioneered using junk mail to sell business software. His name still appears on thousands of direct-mail pieces each month.

Borland is ready to upgrade its image to become a market leader rather than a wily follower. As buyers switch to programs that run with Windows 3.0, Microsoft Corp.'s graphics program, Borland will make its move, Kahn says.

But Borland faces some big chal-

lenges—in the market and in the courts. Lotus, the Cambridge (Mass.) spreadsheet giant, claims that Borland's competing Quattro Pro infringes the copyrights of its best-selling 1-2-3. Last year, Lotus won a similar suit against Paperback Software. And on June 17, Santa

■ Kahn faces a lawsuit from Lotus over a copyright dispute



Cruz Operation Inc. agreed to yank its spreadsheet from the market under an out-of-court settlement with Lotus. Borland, however, has a stronger defense: Quattro Pro is not just a clone of 1-2-3 but has unique features of its own, the company argues. On June 18, a federal judge granted Borland three extra months to respond to a Lotus request to skip the trial and go directly to the question of damages.

The case leaves a cloud over Borland. On fears that it won't be able to respond strongly enough to prevail, its stock dropped by 6, to 45 in mid-June, after

doubling in the past eight months. could be forced to remove a feature that allows Quattro Pro customers to use 13 commands, a key selling point. Analysts figure that damages could run as high as \$300 million, stifling Borland expansion plans and erasing earnings.

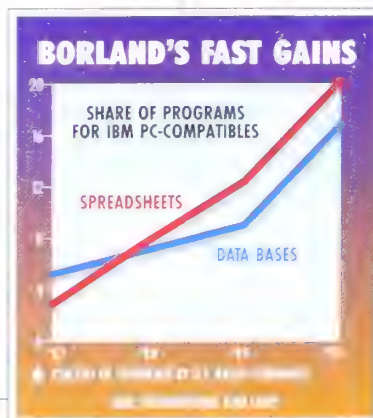
SQUEEZE PLAYS. For now, Kahn is pushing ahead with his Windows program. But in this new market, Kahn may not be as lucky as he has been in the past. His data-base and spreadsheet products gained while competing products from Ashton-Tate and Lotus were sidelined with bugs and delays. Now, Ashton-Tate's Windows data base is expected in December, about the same time as Borland's. And Lotus' Windows spreadsheet is due out at least one quarter before

Borland's. Meanwhile, Microsoft's Excel has a big lead in that market.

Another change in Kahn's barbaric tactics may now draw imitators as well as critics. "We're analyzing what they do," says Ashton-Tate President William Lyons. In 1988, Borland raised eyebrows by offering its \$495 Quattro Pro to Lotus 1-3 customers for \$99. It then sold Paradox for its \$725 data base. Ashton-Tate customers for \$150. "Borland did a superb job of marketing to our customers," admits Donald P. Casey, vice-president of Lotus' Spreadsheets Div. "Kahn was closer to [them] than we were." Now, Ashton-Tate and Microsoft also offer heavy discounts to brand-jumpers.

Barring disaster in the courtroom, still a real possibility—Borland could be on its way to assuming the major role it covets in the industry. It recently got a boost from IBM, which chose Borland's programming tools for its OS/2 operating system. But as Borland grows, Kahn says, "the great challenge is to maintain the barbarian spirit. That's when an uncivilized chief executive comes in handy."

By Richard Brandt
in Scotts Valley, Calif.



THE AGE OF THE
INTELLIGENT SUPER MAP —
THE SMART WAY TO
MANAGE LAND, FACILITIES,
AND PEOPLE

There's a quiet revolution going on. It's a revolution that impacts each of our lives, although few of us have heard anything about it.

affects the rates we pay for utility services and the quality of our roadways. It can influence the speed with which emergency vehicles respond to our calls and how quickly criminals are put behind bars. It can help prevent famine, blight, and pestilence. It has played an instrumental role in planning and fighting wars and then rebuilding war-torn communities. It is being used for applications as far-flung as finding delinquent tax-payers, developing pizza delivery routes, and setting insurance rates. It's even being used to increase the impact of the "junk" mail you receive.

The basis of this silent revolution is a technology called GIS — an acronym for Geographic Information Systems. In the most simplistic sense, GIS technology offers a vastly different approach to the way in which we produce the maps required to manage our communities. Historically, government agencies, utilities, and a long list of private industries relied on manually produced maps to

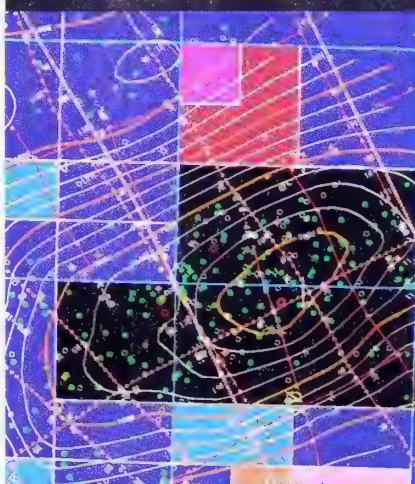
keep track of the property and facilities they manage, as well as the customers they serve. This may sound like a simple task, until you consider that if the maps required to manage a typical mid-size city were stretched end-to-end, they might well extend 20 miles. If you took the hundreds of files describing the features

shown on these maps and stacked them on top of each other, they may well be 100 stories high.

GIS has transformed the world of mapping and facilities management from tedious, error-prone, static pieces of time-worn paper into a dynamic environment that has opened new doors in management effectiveness. Community by community, GIS is relentlessly replacing the piles of maps and drawers of records with modern computer graphics and database technology.

The ability of modern geographic information systems to solve the information overload problems that come with managing mountains of data is benefit enough. However, modern technology has taken GIS a giant step forward. Today's systems go far beyond simply automating map production and management functions. Much larger paybacks lie in their ability to create "intelligent" super maps through which sophisticated analyses can be performed at little more than the

Specialized GIS software performs network routing and trace functions. This type of software is used by moving companies, parcel shipping companies and other delivery businesses to determine optimum routes. Based on cost of travel, this route (shown in blue) was generated for a trucking company in Huntsville, Alabama.



GIS

A TALE OF TWO CITIES

"We all have a stake in the infrastructure problem. I want the city where I live and work to operate properly, and I want it to look good. It's also important from a business perspective to ensure the infrastructure can support continued smooth operation of our business."

JOHN SMALE — Chairman of the Executive Committee of the Board, The Procter & Gamble Company, Cincinnati, Ohio

touch of a button.

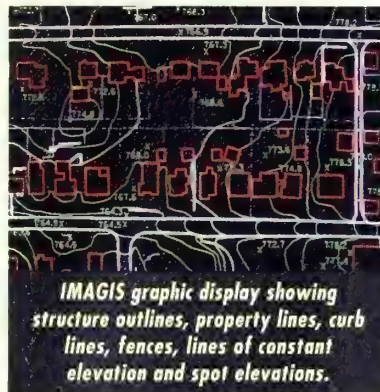
"There's no doubt whatsoever that everyone is impacted by GIS in some way," said Glenn Montgomery, president of UGC Consulting, the largest GIS consulting firm in North America.

"There are massive programs underway by the federal government to do everything from managing forests, to developing defense strategies, to computerizing the Census data that defines who we are, where we live, and what we do. Utilities are using GIS to automate vast transmission and distribution networks. Telephone companies will use GIS to accurately locate every phone in North America. Cities throughout the world are using GIS for applications as diverse as routing sanitation vehicles, replacing water mains, and doing a better job of matching the right equipment to each job. Thousands of private companies are using GIS to make better decisions in areas ranging from

Cities and utilities across North America are searching for better ways to manage the aging infrastructure of streets, water systems, sewers, bridges, and utility networks. And they are working to eliminate the redundant and inconsistent maps and recordkeeping practices which result when multiple departments maintain similar geographic related information individually. In many cases, government agencies, telephone companies, and utility companies are joining together in "multiparticipant" GIS projects to build one common land base that can be shared across a wide spectrum of users. Indianapolis and Cincinnati have set the standard for how government agencies and utilities can join together to save taxpayers and utility ratepayers money while improving the quality of their services.

INDIANAPOLIS

The Indianapolis Public Works Department in 1985 decided to implement a more productive approach to managing the city's infrastructure. What started as one department's effort has grown to include numerous Indianapolis and Marion County government agencies and telephone and utility companies. As a result, some 8.3 million maps, records, and drawings will form the common land base that supports



the needs of such diverse groups as the Public Works Department, Metropolitan Development Department, Transportation Department, Indianapolis Water Company, Indiana Bell, Citizens Gas & Coke Utility, as well as 12 Marion County government agencies.

CINCINNATI

In 1987, Cincinnati's community and business leaders, such as former Procter & Gamble CEO John Smale, got together to develop a comprehensive plan to restore the city's aging infrastructure—representing a \$10 billion investment of 3,000 lane miles of roadways, 100 bridges and viaducts, 25 miles of retaining walls, and a water system that handles 49 billion gallons of water a year.

The city, county, and area utilities joined forces to reduce the cumulative cost and effort of area-wide infrastructure management in a project known as the Cincinnati Area Geographic Information System (CAGIS). At the heart of CAGIS is the development of a common digital land base that will serve the needs of dozens of city and county departments and utilities. As a result of this effort, participants expect to save at least \$11 million over the implementation period.

STEPHEN V. GERARD — UGC Consulting

site selection to marketing to analyzing their competition."

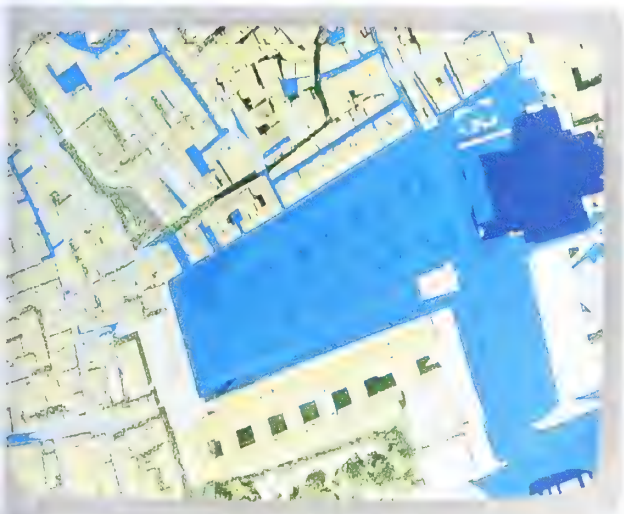
To get a better idea of just how a computerized GIS works, envision a clear plastic sheet onto which the road network for your community has been drawn. Overlay another sheet showing the public works and utility facilities, including the water and wastewater lines, electric and gas systems — then another

showing all property parcels and another with a map of the buildings on those parcels. Then, overlay large-scale features such as elevation, waterways, parks, and vegetation.

You're just beginning to get the picture. Instead of having to view all the information that happens to be on an overlay, a GIS lets users extract only the information that interests them and "overlay" it in any desired combination. In a typical scenario, a public works department gets a call reporting a water leak

The computer screen comes to life and zooms in to the reported location, and with a push of a button, the street appears, followed a split-second later by the water mains and all attached facilities. By pointing to the location where the call originated, the system immediately displays the faulty section of pipe and displays a complete description of that section of pipe, the location of the shut

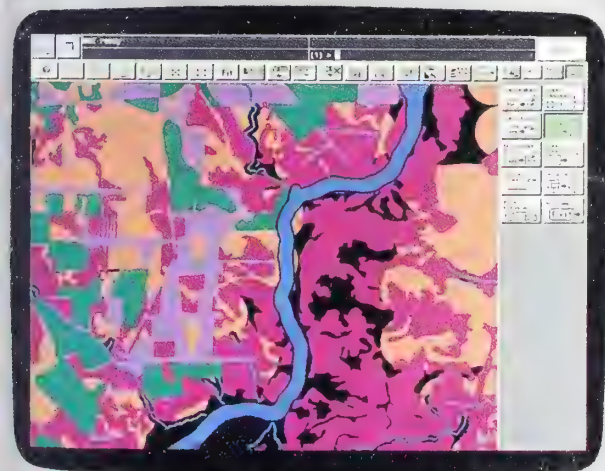
An Organization's Success Depends On Putting Things In Their Proper Places.



Intergraph's GIS is a crucial tool in abatement programs for the city of *Venice, Italy*.

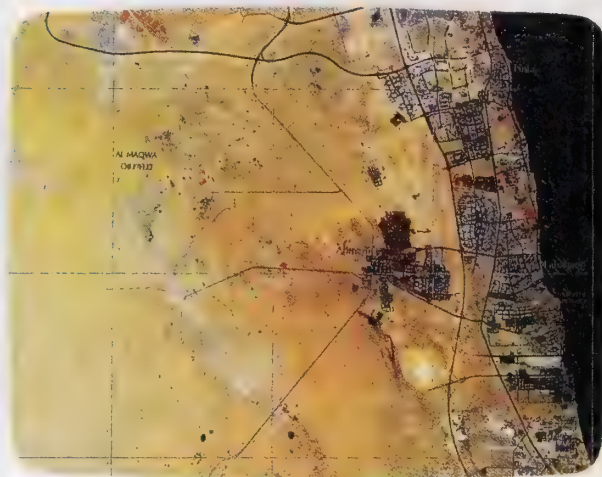
Like buildings, roadways, power lines, and sewer systems. Or rivers, vegetation, mineral deposits, and mountains. All of these features have a proper geographic place. All are part of a Geographic Information System (GIS).

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INTERGRAPH

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GIS

off valve, and a list of all customers that are impacted. Through a link to the city's customer billing system, the system prints out the phone numbers of all affected customers so they can be contacted.

Through GIS, organizations worldwide have the ability to point to any item on the screen and get full details on the history of that feature and the relationship of that feature to anything else in the database. In its ability to extract vast amounts of data in any combination and format, GIS provides the power and sophistication to create multi-dimensional models of our communities, utility networks, and natural resources instead of just static maps. Any point on the earth can now become an index to an unlimited set of information about the land and facilities associated with that point.

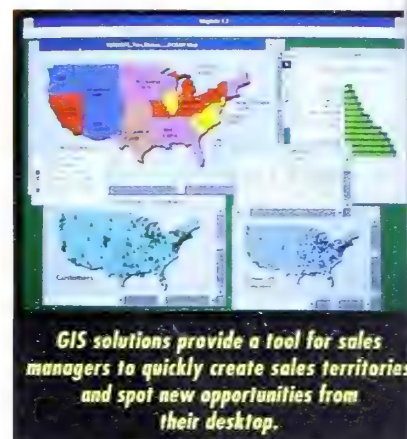
With all this information readily accessible as part of a GIS database, it

becomes a simple matter to ask the system to respond to an incredible variety of requests. When Public Service Company of Colorado wanted to evaluate potential sites for a new transmission corridor

through Denver, they used their GIS to carefully evaluate each alternative, search files for customers who would be affected, and contact them to set up a meeting to determine the most acceptable site to the community. The utility is using its GIS for everything from street-light maintenance to planning customer extensions to maintenance scheduling. CEO Del Hock explained, "We can now detect trouble where we couldn't before and can analyze the performance of individual segments."

When service to 300,000 of its one million customers was interrupted during a massive lightning storm, San Diego Gas & Electric was able to restore power much more quickly than in the past by using its GIS to pinpoint outages and dispatch crews with the right equipment. "From a customer perspective, almost everything we do is impacted by our GIS — from the

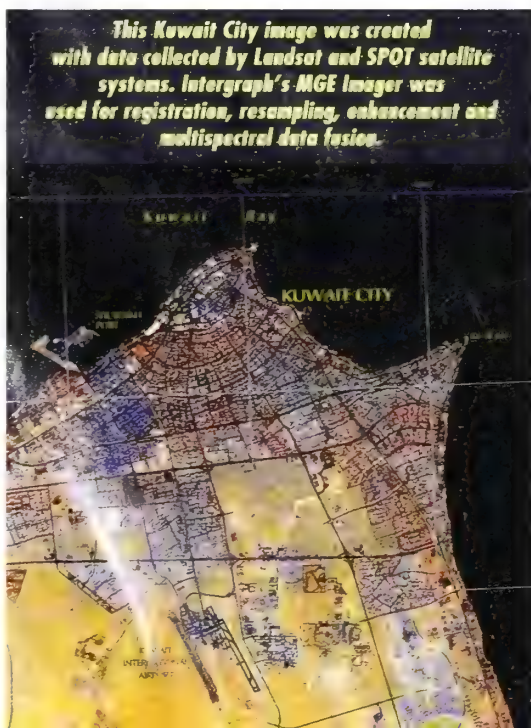
way we're able to respond to them and install service when they request it to helping us analyze a problem on the system so we can respond quickly and repair it," said Don Felsing, vice-president of resource



development and marketing for San Diego Gas & Electric.

When the U.S. Justice Department needed a tool to help it evaluate state proposals for legislative redistricting, it purchased a GIS. Atlanta's Center for Disease Control uses GIS to track eradication of a parasitic disease afflicting 10 million people annually. In Ontario, an A&P grocery chain is using GIS to analyze shopping patterns and store market share; it also uses the system to plan new store locations. Traveler's Insurance employs a GIS to market its insurance and physicians' networks by relating doctors to a business' employees. Even Coca-Cola uses GIS to help analyze the "cola wars" and assess how various products are doing in different distribution channels.

These are just a few of the thousands of uses of GIS. "In coming years, GIS will not just be the system of choice for utility companies and government agencies," said Denny B. Sigloh, IBM's director of Geographic Information Systems. "it will be the system of necessity for banks, insurance companies, retail stores, schools, airlines, petroleum companies... it could go on and on. GIS is fast becoming a mainstream solution to everyday chal-



MANY ARE CALLED FEW ARE CHOSEN

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obvious paths are crowded with me-too approaches. Positions of leadership take foresight and tenacity. Many companies now use GIS; so how do you get the edge? Shared vision.

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GEOVISION

GIS

allenges faced by a great many people and will, no doubt, be the basis of countless applications we've not yet dreamed of."

"The bottom line is that companies are purchasing these systems to save money or make money," said Doug Gerull, vice-president of the Mapping Sciences Division for Intergraph Corporation, one of the largest GIS vendors. "For companies whose wealth is derived from assets that are land-related, GIS is a tool to maximize the value of these assets through better management. On the other hand, the technology has another value as a strategic tool through which new avenues of business opportunities can be found."

Market Perspective

GIS represents one of the fastest-growing of computer technologies. Depending on whose estimates you look at, GIS purchases could reach anywhere from \$5 billion to \$7 billion by the end of 1991. According to UGC Consulting's Montgomery, whose firm conducts research on activities and trends in the GIS market, "Currently, some one-third of the larger gas and electric utility companies, cities, and counties in the U.S. already own a GIS, and almost every large organization that doesn't own a system plans to purchase one. In the telephone industry,

the percentages are even higher."

There are over 10,000 cities and counties in the U.S. alone, and every city and county in the world is a prospective user of GIS technology, as are all of the utilities that serve them, countless state and federal agencies, and every private company that must make strategic decisions based upon where customers are located.

The operational improvements gained through GIS have many benefits to the citizens served by the organizations who are using these systems. One benefit is

seen in the rates we pay for our services. Over the life of the system, a GIS can often save millions of dollars in productivity gains — savings that are passed on to ratepayers in the form of cost containment. "Any time you have productivity improve-

ments by the organization, they will be reflected back to the customer," says Robert Forsyth, president and CEO of Synercom Technology, Inc. "These systems are having enormous impact in helping people increase productivity. Using these systems, one can increase the

amount of work a person can accomplish, lower the cost of doing that work, tremendously increase the accuracy, and maintain the long-term survivability of the information, which can be used over and over for literally decades." Other benefits that accrue are more difficult to measure but are just as significant. Public works officials are able to respond to emergencies and restore service more quickly. Potholes are filled more rapidly. Trash removal is more expeditious. Ambulance and fire service is more responsive. Tax reassessments are more timely.

Public safety is another area in which GIS has vastly improved the quality of service. It is being used by small and large communities for activities ranging from monitoring the spread of disease, to

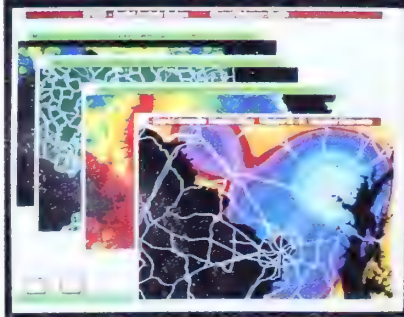


MODERN TECHNOLOGY OFFERS BETTER UNDERSTANDING OF ANCIENT TIMES

In 24 A.D., the violent eruption of Vesuvius wiped out the flourishing city of Pompeii. Today, GIS technology is being used to bring the ancient culture back to life, offering a remarkable view of life as it existed over 2,000 years ago.

IBM is working with the Soprintendenza Archeologica di Pompeii and Fiat to "recreate" Pompeii and the richness of its archeological history. GIS technology and three-dimensional modeling are being used to catalogue over 8,000 excavated frescoes and numerous mosaics, as well as detailed information on 22,000 pages of catalogue entries describing excavation activities from 1862 to date. The vast database of information offers scientists and laypersons alike an enormous resource for better understanding Italy's rich cultural heritage.

GIS brings together and analyzes different types of information to support the decision-making process. For example, the screen shot below shows a number of map overlays which were used to select a new hospital site.



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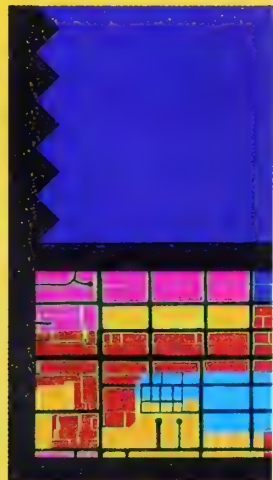
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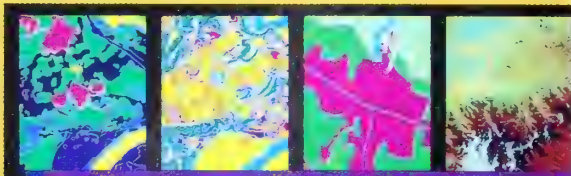
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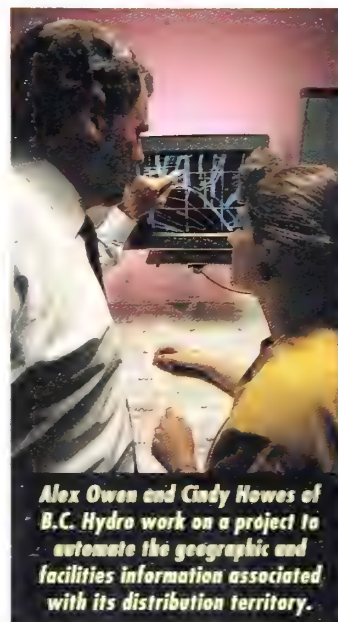
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dispatching emergency vehicles, to crime analysis. In San Francisco, programs like the Youth Environmental Study (YES) uses GIS to analyze AIDS occurrences and agency outreach and control efforts. Also in San Francisco, GIS was used to assess the damage caused by the 1989 earthquake and to help locate fires and plan access routes into and out of ravaged areas. In dozens of cities like Syracuse, N.Y., information on victims, suspects, location, and other details of area crime are analyzed weekly and monthly with a GIS to determine criminal patterns so that units can stake out areas showing heavy activity.

According to Jack Dangermond, president of the Environmental Systems Research Institute (ESRI), a leading GIS technology vendor, "GIS offers an invaluable tool not just in analyzing crime but in helping us understand it as more than a single-dimensional problem. In reality, crime doesn't stop or start because we put more police on the streets. It has to do with jobs, equal opportunity in educa-

tion — many different dimensions. Crime is very integrated with the whole network of the way we do things as a society, and we need more complex, inter-related institutional approaches to address those problems. GIS will help make this happen.

In the telecommunications industry, companies like Southern Bell, British Columbia Telephone, and Southwestern Bell have implemented GIS



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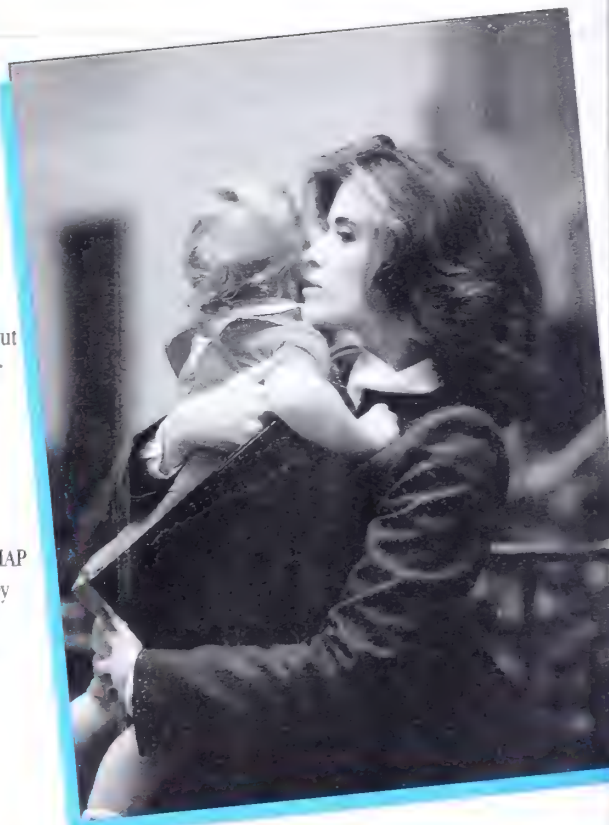
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projects that are resulting in big benefits for these companies. U.S. West and Ameritech have similar projects underway as do numerous other companies. More and more telephone companies use GIS to decide where to install fiber cable, "based upon system usage, customer demographics, and other variables," said Doug Seaborn, president of GeoVision, which markets a GIS for telephone applications. "These systems are then used to help design the network, determine where to bury the cable, how deep it should be buried, and all sorts of important engineering considerations that can, through GIS, be done in a standardized and more efficient way."

Numerous federal and state agencies rely heavily on GIS for a variety of purposes ranging from strategic defense, to managing natural resources, to routing postal vehicles. The U.S. Department of Justice recently purchased a GIS to evaluate state redistricting plans, and many states are using GIS to analyze and select among multiple redistricting alternatives. In the Persian Gulf, the Depart-

ment of Defense used GIS to support the mapping efforts of Operation Desert Storm, and GIS technology is currently being used to reconstruct war-torn Kuwait City, in spite of Iraq's theft of the city's

GIS hardware — a duplicate database was stored safely in Japan.

According to Dr. H. Dennison Parker, publisher of GIS World, the industry's leading GIS publication, "The Bureau of Land Management plans to spend over \$200 million in the next few years to modernize the U.S. public land database. The Forest Service plans a project similar in scope and size. These are just starting points for these projects; they may well reach over \$1 billion each by the turn of the century. If you consider the GIS procurement plans of other agencies, we anticipate procurements of around \$6 billion by the year 2000, and that's just the projects we know about."

Forecasts for GIS are Open-ended

There are literally thousands of GIS users today. As the technology continues to migrate to less-expensive machines and the software becomes easier to use, GIS use will inevitably extend to more and more people. With the increasing numbers of off-the-shelf, ready-to-use databases becoming more popular and

providing access to incredible amounts of geographically referenced information at the touch of a button, the number of users could swell to hundreds of thousands in the next few years. "Most organiza-

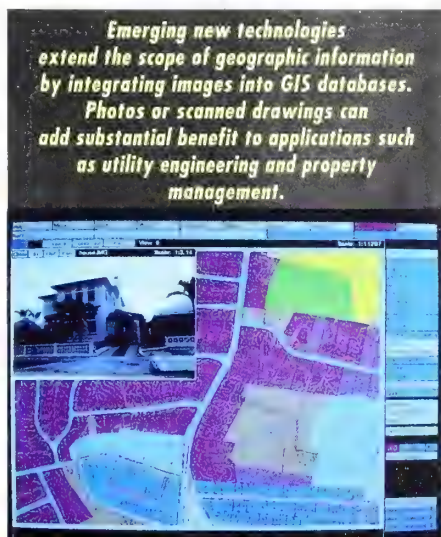
tions are suffering from information overload," said Giulio Maffini, president of U.S. Operations for TYDAC Technologies. "They have treasures of data that they're collecting every day that is virtually

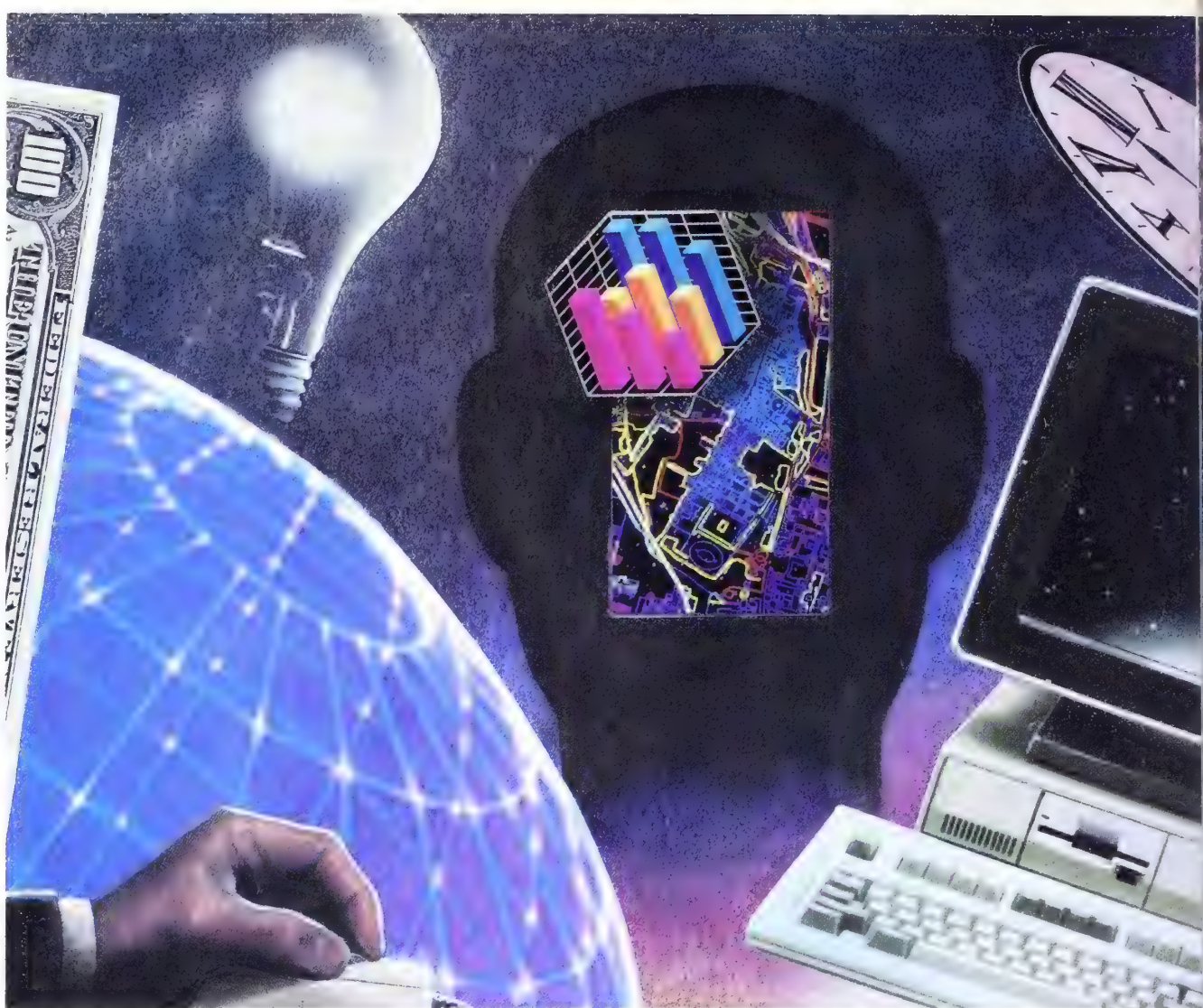


impossible for an individual to synthesize. GIS reduces these murals of data to comprehensive and compact images which are easy to understand."

From the mundane to the esoteric, GIS is about almost everything we do. It's about building new subdivisions, dispatching ambulances, and managing our forests. It's about preventing the spread of disease, mitigating environmental damage, and doing a more effective job of marketing. GIS touches all of us in some way and will continue to weave its way into the fabric of our society as more and more people come to recognize the power it holds as a tool for better management of our businesses, our infrastructure, our natural resources, and even our personal lives.

Text written by Ginger M. Juhl in association with UGC Consulting, Englewood, Colorado. Design by Parham Santana Inc., NYC.





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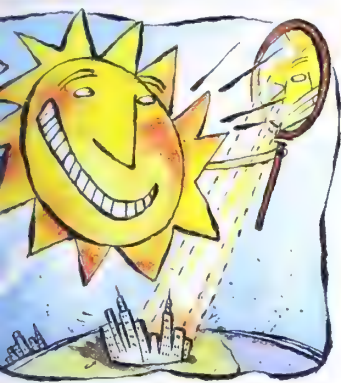
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Developments to Watch

EDITED BY WILLIAM D. MARBACH

BRIGHT IDEA SOLAR ENERGY



This so-called heat-pipe approach will prove "the key to large-scale use of solar energy."

Weizmann's pilot plant has 64 giant, computer-controlled mirrors that focus sunlight on a methane-filled tank atop a tower. As the methane absorbs the sun's concentrated heat, it breaks down into hydrogen and carbon monoxide. This hazardous mixture, called synthesis gas, can be stored or piped to distant customers. Then, a chemical reaction converts the gas back into methane, liberating enough heat to produce steam, which can be used to generate electricity. Meanwhile, the constituted methane will be piped back to the solar plant, therefore allowing the cycle to be repeated in an endless loop. The \$1 million pilot plant will undergo three years of testing. If it works, the next steps will be a small prototype, then a commercial plant.

THIS WING WARMER MAY MAKE FLYING SAFER

In winter, ice forming on an aircraft's wings is a dangerous problem for pilots, who now rely on chemical de-icers. Someday soon, though, they may be able to flip a switch instead. 3M Corp., a division of International Paper Co., and Thermion Inc. have developed a system that uses an extremely lightweight, conductive fiber mat that can be embedded in paint on wing surfaces where ice builds up. An electronic controller connected to the mat provides heating and system monitoring. Made of nonwoven, nickel-coated graphite fibers, the material weighs just one-third of an ounce per square yard, so it doesn't cause extra drag. The Electro-Thermal Anti-Ice System can be installed on older planes, and is likely to cost \$50,000 per plane such as the McDonnell Douglas MD-80. American Airlines Inc. plans to try out the system on a decommissioned plane in September. Thermion expects Federal Aviation Administration approval after 12 to 18 more months of testing.

NOW, CHEST SURGERY COULD BE EASIER TO BOUNCE BACK FROM

Surgery inside the chest is typically so traumatic that the average hospital stay for thoracic surgery patients is 7 to 10 days, including several in the intensive care unit. And it may be two months before the patient returns to work. But a new technique could radically reduce the recovery period. In so-called endoscopic thoracic surgery, a miniature

video camera is inserted into the patient's chest through a small incision. During the operation, images from the camera are projected onto a monitor that becomes the surgeon's window into the body. With this technique, patients have been released as early as the second day after surgery, with no time spent in intensive care. And they may return to work in as few as 10 days.

So far, the endoscopic surgery has been very effective in performing biopsies, removing tumors, and removing fluid from around the heart. It has not yet been used in the more complicated heart surgeries. "This is still in its embryonic stages," says Dr. Ralph Lewis—chief of thoracic surgery at St. Peter's Medical Center in New Brunswick, N.J., and clinical professor of surgery at the University of Medicine & Dentistry of New Jersey—who is pioneering the technique.

A DATA BASE THAT LETS YOU BROWSE FOR AN EXPERT

Searching for a scientist who is making new polymers to deliver drugs? Or perhaps you want to tap into research teams fabricating diamond films or using transgenic animals to study Alzheimer's disease? Now, there's a data base for all this. Cartermill Inc. in Baltimore has created a service called BEST North America that tracks the scientists, facilities, and patent records of 90 universities.

"We believe this is the best way for corporations to connect with university expertise," says Kenneth C. Blaisdell, Cartermill's president. Some 20 companies, including Amoco, Kodak, and United Technologies, have signed on. Fees range from \$6,000 to \$25,000 per year for unlimited browsing time.

NO-FRILLS BURIAL FOR HAZARDOUS WASTE

Cleaning up hazardous waste sites continues to be a headache, partly because the cost of removing contaminants is so high. Terran Environmental Inc., however, has a process that may cut the costs by entombing the waste in plain old calcium carbonate, which is found in limestone.

The first step is to inject a calcium carbonate solution around and below the toxic waste site. Within days, the calcium carbonate develops a mud-like consistency that bonds to the existing rock or other surrounding material. Then, over a period of months, the calcium carbonate hardens into rock, becoming an impermeable weld that prevents the hazardous material from leaching into ground water. But the process requires that the material surrounding the barrier be naturally or artificially kept in an alkaline state.

Terran's executives say the technology could be used to prepare ashes for landfill disposal, entomb mine tailings, seal existing hazardous waste or landfill sites, and even bury radioactive waste. Sealing a waste site with the new process, they say, could cost at least 60% less than other methods. New York regulators and the Environmental Protection Agency have granted the Canastota (N.Y.) company permission to test the process at a site in New York State.



INSTEAD OF STAR WARS, LITTLE STAR WARS?

Congress considers a downsized SDI based on existing technology

When Ronald Reagan dreamed, it must have been in Panavision. So in 1982, when a group of breathless defense advisers pitched a scheme to knock ballistic missiles out of the sky, the President was more than receptive. Soon, Reagan was telling Americans about a space shield that would render nuclear weapons "impotent and obsolete."

Star Wars was a typical Reagan idea. It was big. It was bold. And its cinematic sweep glossed over potentially insurmountable details such as cost and technical feasibility. In the more prosaic and tight-fisted world of the Bush Administration, the Strategic Defense Initiative lives on. But the plan now being debated in Congress is vastly slimmed down to fit the much-reduced Soviet military threat and the shrunken national purse.

Star Wars Lite, as it might be called, gives up the notion of stopping the sort of all-out Soviet nuclear attack that now seems wildly improbable. Officially called Global Protection Against Limited Strikes (GPALS), its goal is to shield the U.S. from a renegade or accidental attack by up to 200 Soviet land- or sea-launched missiles—and to knock out cruder missiles that might be lobbed by a future Saddam Hussein.

SLAM DANCE. This downsized SDI eliminates some of Star Wars' most daunting challenges. Gone are such problematic technologies as X-ray lasers, particle beams, and giant orbiting mirrors. And while GPALS (pronounced as a friendly sounding Gee-Pals) still faces plenty of engineering challenges, it derives mainly from existing technology. As envisioned, the defense relies on a network of spotter satellites (Brilliant Eyes), advanced ground-based missiles, and space-based rockets (Brilliant Pebbles) that would kill ballistic missiles through kinetic energy—the sheer force of

impact. "The technology is well-understood, available, and could be deployed in the mid-'90s," says William C. Loomis, director of defensive missile systems at Lockheed Corp., the biggest Star Wars contractor.

Even SDI's critics, while quibbling with Loomis' schedule, reluctantly agree. "Most of these gadgets will work about as well or as poorly as anything else [defense contractors] make," says John E. Pike, space-policy expert at the dovish Federation of American Scientists.

Compared with Reagan's full-blown Star Wars program, which some analysts said might cost as much as \$1 trillion, GPALS carries a cut-rate price tag. Costs over the next 15 years, including operating expenses, are pegged at \$120 billion, not including the \$23 billion spent on Star Wars research since 1983 (table). But Congress is choking on even this bargain-basement number. The House has already voted to cut \$1.7 billion from President Bush's \$5 billion request for fiscal 1992. The savings would come mainly from killing Brilliant Pebbles, the part of the plan that would put 1,000 rocket-bearing satellites in orbit, ready to blast attacking missiles. But eliminating these, says SDI Director Henry F. Cooper, is "a direct assault on the entire concept."

In a slap at Cooper himself, the House has also voted to wrest a large chunk of the GPALS program from his office and hand it to the Army, which has been managing ground-

based missile development. GPALS could face rough going even in the traditionally more sympathetic Senate, where Republicans John W. Warner of Virginia, Richard G. Lugar of Indiana, and William S. Cohen of Maine have urged the White House to show more flexibility in negotiating with critics lest too rigid a demand from Bush for funding of space-based weapons kill the whole program.

But Cooper and other SDI backers see the space-based weapons as critical. They envision GPALS as a multilayered system with satellites forming the first line of defense. Here's how it would work: Say a group of renegade Soviet officers launches a volley of 50 nuclear missiles toward Los Angeles and Chicago. Orbiting Brilliant Pebbles satellites that use heat-seeking sensors and on-board computers target the missiles in their boost phase. They quickly fire guided "kill vehicles" about the size and shape of a big oatmeal box to slam into the vulnerable missiles at high speeds, smashing them to pieces on impact.

The missiles that escape drop their boosters, releasing clouds of warheads and decoys to sail through outer space. At that instant, Brilliant Eyes satellites

WAR IN SPACE

The latest version of the STAR WARS defense would rely on a network of radars, ground-based missile sensor satellites, and killer satellites

BRILLIANT EYES

These spotter satellites would identify and track missiles between launch and reentry into the atmosphere

Prime contractors for early development: TRW, Martin Marietta, Rockwell, Lockheed



GSTS Ground-based Surveillance and Tracking System

These heat-detecting telescopes would remain grounded until an emergency when they would be launched to help monitor an enemy attack. McDonnell Douglas

click on to pick out the phonies. At the same time, pop-up telescopes called Ground Based Surveillance & Tracking System (GSTS) are fired from the ground to fill gaps in the satellite coverage, while more Pebbles fire at the warheads.

CLEANUP BATTERS. Meanwhile, dozens of Ground Based Interceptors (GBI) launched from the U.S. use their own seekers to target warheads and fire their own kill vehicles. Another set of ground-launched defenders, called endoatmospheric/exoatmospheric interceptors (E²I), takes out remaining warheads as they enter the atmosphere. Ground-based radar and elaborate battle-management computer systems tie these weapons together. If all works as intended, Los Angeles and Chicago are saved.

GPALS also includes "theater-based" defenses small enough to be airlifted to a war zone—and deal with both sophisticated tactical missiles and Third World rockets that might fly too low to get within Brilliant Pebbles' range. The systems would be similar to the Scud-busting Patriot of gulf-war fame, but smarter and more powerful. LTV Corp.'s Extended Range Intercept Technology (ERINT)—pronounced ee-rint) will cover a territory three to four times as large as the Patriot does. ERINT is also smaller

and quicker—16 will fit in a launcher built for four Patriots. Most significant, ERINT won't have a warhead—it will destroy an incoming missile by ramming it.

That's a big improvement. Although a warhead such as Patriot's can knock a missile off target without scoring a direct hit, the blast won't always destroy the missile. In Saudi Arabia and Israel, that meant that damaging debris—and sometimes the Scud warhead itself—rained on people and buildings. ERINT would smash the target and itself to smithereens high in the sky. Its developers are experimenting with aluminum and other reactive materials that would burn—and take chemical or biological bombloads with them. To meet the need for pinpoint accuracy, engineers have put a bullet-like spin on the ERINT, which requires some fancy computer tricks. While the missile rotates, its radar spins with it. On-board processors would compensate for the motion, making the radar act as if it's stationary.

For an extra layer of protection atop the ERINT and Patriot systems, Theater High-Altitude Air Defense (THAAD) missiles would rocket to the atmosphere's upper reaches. Analysts say THAAD will likely protect an area about a thousand miles square and travel so high that exploded chemical or biological substances dissipate before reaching the earth.

THAAD, which is being developed as a theater-based weapon, too, could be deployed by 1995. But because it could also be used to defend against strategic missiles, its testing will soon brush up against the 1972 Anti-Ballistic Missile (ABM) Treaty with the Soviet Union, which bans testing or deployment of most strategic-missile defenses.

Indeed, the ABM treaty looms as a major political hurdle for GPALS. Many of its elements,

including several ground-based interceptor systems, could pose treaty problems, concedes James D. Carlson, deputy director of the Pentagon's SDI organization. And any Administration move to abrogate the treaty would set off a fire storm on Capitol Hill.

Plenty of engineering challenges also lie ahead, though no one is deriding GPALS as a science-fiction fantasy. The thorniest problem is distinguishing warheads from decoys in space. "We're at the crawling stage" in trying to tell them apart, says James C. Katechis, manager of the Army's GBI interceptor project.

Once the warheads reenter the atmosphere, the problem becomes easier to solve, since the decoys, being lighter, are slowed more by drag. If researchers can't find a way to tell warheads from decoys in space, SDI could dump GBI and buy more E²Is—the interceptor that can operate in the upper atmosphere. But that presents its own difficulties. High speeds and air friction will combine to make the interceptor white-hot. So its infrared sensor must peer through a sapphire window cooled by a flow of liquid nitrogen, while a computer adjusts for the resulting distortion. That makes the E²I much more expensive than GBI.

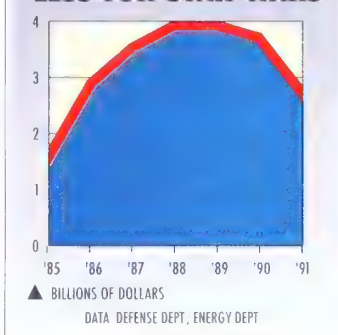
CHURN 'EM OUT. Another challenge is building 1,000 Brilliant Pebbles satellites for less than \$1.5 million each. Satellites have always been handcrafted one or a few at a time—and they typically cost \$100 million or more apiece. But Brilliant Pebbles will have to be built assembly-line style. So contractors are trying to combine their missile production expertise with satellite-building knowledge to make it work.

Such problems may be difficult, but they are far less daunting than the obstacles facing the original Star Wars plan. Now, the big question is Congress. Senate opposition to Brilliant Pebbles appears strong. And if the Senate goes along with the House, GPALS faces a setback. "The technology is at hand," says Lieutenant General Robert D. Hammond, commander of the Army's Strategic Defense Command. "It's just a question of commitment and resolve."

And politics. And money.

By Russell Mitchell
in Washington

LESS FOR STAR WARS



BRILLIANT PEBBLES

Thousands of these satellites would orbit in the skies, ready to fire kinetic weapons to destroy enemy missiles. Martin Marietta, Hughes



GROUND-BASED MISSILES

During an attack, high-flying missiles would blast into space to destroy incoming warheads. Lower-flying missiles would shoot down surviving warheads as they reenter the atmosphere. Lockheed, McDonnell Douglas

DATA BW



AMERICA'S CUP



SKIPPER KOCH: "A LOT OF PEOPLE SAY THAT I'M NOT GOOD ENOUGH TO WIN"

NOW, IT'S BILL KOCH VS. THE SEA

He's rich, tough—and he's taking on Dennis Conner for the cup

Bill Koch has always been an outsider. As a child, he says, he endured the baiting of his two brothers, who later shut him out of managing Koch Industries Inc., the family's privately held oil empire. As a 40-year-old, Koch waged a proxy fight against them for control of the business. The bid failed, but the brothers paid him \$550 million to go away. Eleven years later, Koch is again fighting for attention. Only this time, he's trying to elbow into the elite club of yacht-racing champions.

He has budgeted \$40 million for an admittedly long-shot bid to represent the U.S. in next spring's America's Cup races. Outspending sailing superstar Dennis Conner by \$15 million for the right to defend the cup, Koch hired away the world's best sailors—including former Conner crew members. And he's building three ultra-high-tech yachts designed by aerospace physicists and manufactured at Hercules Aerospace Inc.'s missile plant in Magna, Utah.

Should he beat Conner, Koch (as in "coke") would be the first owner to skipper his own cup entry since Ted Turner won in 1977. But where Turner was ribald and hard-drinking, Koch is austere,

piloting his newest boat, the Jayhawk, in almost total silence. "When I sailed with Ted Turner [in 1977], we played together and partied together," recalls Gary Jobson, Koch's co-skipper and tactician. "Bill wants to be one of the guys, but he doesn't let people get too close."

FANCY DIGS. As a sailor, Turner's long suit was charm. Koch's is money. His 38 white-uniformed sailors tone their muscles daily in a gleaming gym on the America's compound, complete with a trainer who used to work for the San Diego Chargers. Following a 7 a.m. workout, the crew feasts on a lavish spread of low-fat gourmet goodies.

The sailors have pretty fancy digs offshore, too: a trio of \$5 million, 75-foot carbon-fiber boats, of which the Jayhawk is the first. That craft is a sleek, efficient sailing machine, moving nearly as fast as the wind that powers it. It's stuffed with electronics, including digital readouts of sail tension. When Koch tells his trimmer to "reduce tension on 1 to 7.8," he's ordering him to ease up a bit on the huge Kevlar mainsail.

Don't look here for a description of the boat's hull and keel, though. Koch is a secrecy fanatic, foiling scuba-diving

spies with a special dock with corrugated metal sides that extend to the bottom of San Diego Bay.

Koch trained as a chemical engineer at the Massachusetts Institute of Technology, and his hull designs have won the competition. One of his boats won last year's Maxi Worlds races for large yachts, prompting Koch to ask San Diego Yacht Club officials if they wanted to use his design for their cup defense. The club was interested—as long as Conner skippered the boat. Koch nixed that idea and entered the fray himself.

Even with his superior boat, Koch will have a tough time catching Conner. A sailor for only eight years, Koch understands why "a lot of people say that I'm not good enough to win. Conner is more experienced. In equal boats, I would not stand a chance against him."

But Koch has a knack for combining technology with talent. "It's not just our helmsman against another helmsman. It's the total program," says Jerry Dow, executive vice-president of Teac Dennis Conner. "We respect Bill—he's put together a first-rate team."

Koch commutes from San Diego to West Palm Beach, Fla., for a few days each month to pilot Oxbow Corp. Teac, a private energy company, which Koch says has annual revenues of \$500 million and "quite respectable" return on equity, sells electricity from its Nevada geothermal plants to utilities in Southern California. He says he wants to keep Oxbow small to qualify for tax breaks for alternative fuels.

LAWSUITS GALORE. Tensions within the Koch family have an electricity all their own. In March, Koch contested the will of his mother, who left him out of her \$10 million estate. While his mother was still alive, he sued her over the terms of the family's charitable trust and subpoenaed her to testify even though, claiming family lawyer, she had just suffered a serious stroke. Koch maintains that his mother was well enough to play tennis at the time of the suit. And in a separate action, Koch is suing his brothers, claiming they undervalued assets in the settlement that left him with half a billion dollars. "It's beyond vindictive," says Donald L. Cordes, general counsel of Koch Industries. "It's an abnormal, desperate bitterness."

Koch contends he sold his shares for about half their value. "There's a tremendous amount of money involved, and I hate to get screwed," he says. "It's not about sibling rivalry." Whatever his motivation, Koch doesn't shy away from a fight. Dennis Conner better tighten his topsiders.

By Eric Schine aboard the Jayhawk

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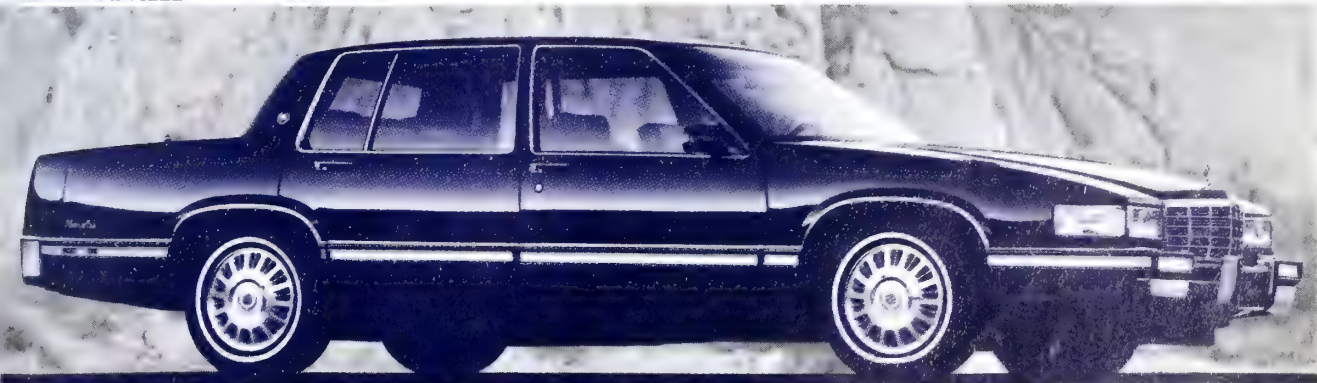
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CEO DUNLAP
MADE QUITE A
BUNDLE FROM
GO-VIDEO

THE DOUBLE-DECK WOES OF GO-VIDEO

Its antitrust suit flopped, and its VCR-2 is getting a chilly response

You've got to hand it to R. Terren Dunlap: The man isn't afraid to create a stir. In 1987, the brash chairman of tiny Go-Video Inc. dragged 17 of Asia's consumer electronics giants—including Sony, Matsushita, and Samsung—into court. He charged them with conspiring to keep Go-Video's fancy dual-deck videocassette recorders off the market by refusing to manufacture the product on a contractual basis. Why? This powerful Asian cartel wanted to snuff out Go-Video's Yankee ingenuity, Dunlap argued.

Unfortunately for Dunlap and Go-Video investors, the company recently lost its \$750 million antitrust suit against three Japanese electronics companies—Sony, Matsushita, and JVC—that hadn't yet settled with Go-Video or been dropped from the lawsuit. Now, Go-Video's

VCR marvel is on the market. And the former trial attorney must prove that his claims of Yankee innovation weren't so much hot air.

It won't be easy. Dunlap, 46, can no longer rely on a stream of legal settlements and stock offerings to prop up the

company's finances. And the outlook for the VCR-2 isn't encouraging. Last fall, Go-Video finally launched its heralded dual-deck VCR after reaching a pact with Korean electronics major Samsung Group to turn out the machines. However, the VCR priced at an eye-popping \$1,000, hasn't attracted many wheeled video freaks. Even if it did, a Japanese rival such as Sony or JVC with stronger technology and capital could quickly roll out a superior model.

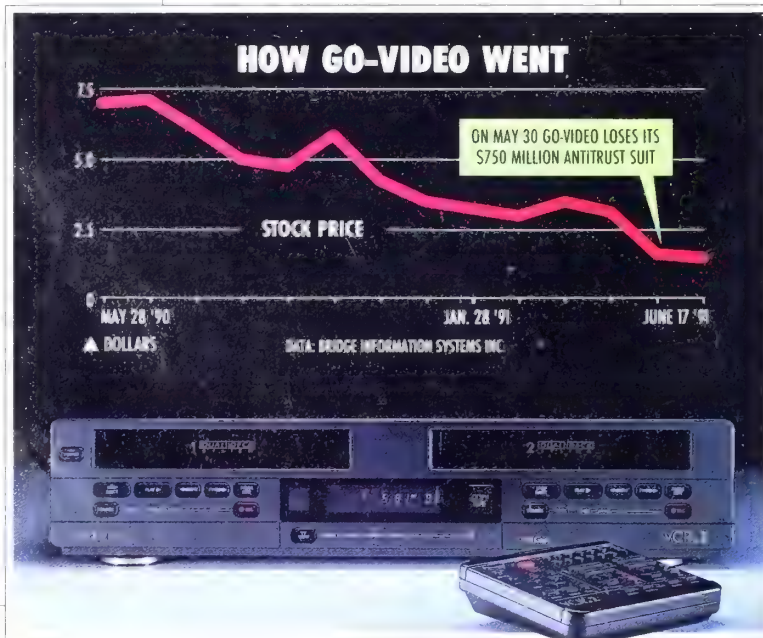
Now that the promise of a big legal payout on hold while Go-Video appeals the antitrust verdict, Go-Video investors

have taken a beating. The stock plunged 43%, to 15¢, when the trial ended on May 30, and has shed about 75% of its market value during the past year. However, Dunlap has made quite a bundle at Go-Video. He took the company public in 1986, and its stock rocketed 24 by mid-1988. Dunlap netted a \$3 million profit by selling 158,000 Go-Video shares in 1988 and 1989. And he still holds a 5.6% stake in the company, mostly through options.

BIGGER ROLE. To turn things around, Dunlap is now restructuring operations, revamping his marketing plan, and reaching out to mass-market electronics distributors. In the hope of luring more recession-wary buyers, he lowered the VCR-2's list price to \$799. Dunlap also says his team will now devote "98% of our energy to marketing the VCR-2."

He will certainly play a bigger role in day-to-day management: On June 10, Go-Video President Eric J. Schedeler signed suddenly, though he will play a role in marketing VCR-2 overseas. It's quite a toy: The VCR-2 can copy a videocassette onto another tape, edit tapes, and record two programs at once.

But by cutting the price of the VCR-2, Dunlap has taken a big bite out of Go-Video's already slim—12¢ or so—gross



profit margins. So, Dunlap also plans to eliminate one-quarter of the company's 8-person payroll and scale back its research and development spending by 10%. Go-Video has been working on a wireless system to connect VCRs with TV sets, but the VCR-2 is its only growth vehicle.

That's a problem. The VCR-2 has received decidedly mixed reviews. Although the machine has won some praise for making it easier to copy tapes, it has drawn fire for its lack of high-fidelity sound, fancy editing functions, and slow-motion display. "Basically they're trying to sell a box with two low-end machines in it," says David Lachenrue, editorial director of *Television Digest*. Also, anyone can fashion their own dual-deck recorder by simply wiring two \$200 VCRs together—at about half the price of Go-Video's VCR-2.

Indeed, the product's initial \$1,095 price tag really turned consumers off. Although the VCR-2 was sold by elite shops such as The Sharper Image and Hammacher Schlemmer, videophiles didn't rush to buy. Go-Video shipped about 16,000 units last year, and a little more than 2,000 additional units since then for total sales of \$11 million. Sadly, that hasn't been enough to stem Go-Video's steady stream of losses—\$8 million in all—since 1987. True, Go-Video posted its first profit ever of \$1.4 million in its recent quarter. But without the addition of \$4.8 million in legal settlements the company would have had a loss. In the past, the company has garnered nearly \$25 million in such settlements and stock offerings to boost its financial position.

GAG ORDER. Numbers such as those aren't what Dunlap had in mind in the early 1980s, when he and a partner came up with the idea for the VCR-2. With no major U.S. companies in the VCR field, Dunlap approached virtually every major Asian manufacturer about making the VCR-2. They all refused, citing the machine's limited appeal. The irrepressible Dunlap, though, saw a conspiracy in the works. During the trial, he grew so vocal in his criticism of his Asian rivals that U.S. District Judge Robert C. Broomfield slapped a gag order on him.

If Dunlap's crusade is to continue, he had better broaden Go-Video's market reach. The company has lined up mass-market retail chains such as Silo and Highland Superstores to carry its lower-priced VCR-2. It has also launched a new advertising campaign, trumpeting the user-friendliness of the machine's copying abilities. But for Go-Video to prosper, it will need to develop a wider audience of tape-heads. If not, Dunlap may have to hit the reset button on his dreams of building Go-Video into a force within consumer electronics.

By Kathleen Kerwin in Scottsdale, Ariz.

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PFIZER FINALLY SEES ITS PAYOFF

Heavy R&D spending dragged down earnings—until now

Not too long ago, you'd have had a devil of a time finding a Wall Street money manager with many kind words for Pfizer Chairman Edmund T. Pratt Jr. Back in 1989, analysts skewered the longtime CEO for doing precious little to boost the company's flagging stock price or sliding earnings. What really sent their blood pressures soaring, though, was the fact that Pfizer Inc. hadn't launched a major new product since 1982. In fact, some investors were hanging on to Pfizer stock as a possible takeover play.

Two years later, Pfizer has a new CEO—William C. Steere Jr.—and a pipeline full of promising new drugs. And, ironically, much of the credit goes to Pratt, who continued to pump cash into Pfizer's research-and-development efforts despite the dampening effect on the company's earnings and stock performance. "We were getting roasted by

analysts when we were investing in R&D during the '80s," says Steere. "Now, we're seeing the payoff."

And how. Pfizer has rolled out three new drugs during the past two years and has another six applications pending with the Food & Drug Administration (table). One sign of more robust times at Pfizer: In 1988, new products—those on the market for less than two years—accounted for just \$166 million in sales. They will contribute 10 times that amount this year. "Pfizer has the best product line of any drug company," says William F. Harnisch, president of Forstmann-Leff Associates Inc., an institutional investor.

HUGE MARGINS. Outsiders also like what they see in Steere, who formerly ran Pfizer's \$3.2 billion pharmaceutical unit. A former sales representative, Steere is more collegial than the fiercely independent Pratt, who will stay on as chairman

until next year. The 54-year-old Steere will continue Pratt's basic strategy of spending heavily to build up Pfizer's new-product portfolio.

And why not? New drugs are the lifeblood of a pharmaceutical company. They usually have higher profit margins than older drugs, which often face intense price competition from generic rivals. However, Steere is likely to differ from Pratt in one important respect: He will focus more on Pfizer's core health care business, which accounts for 68% of the company's \$6.4 billion in sales. He may also jettison some low-margin Pfizer businesses.

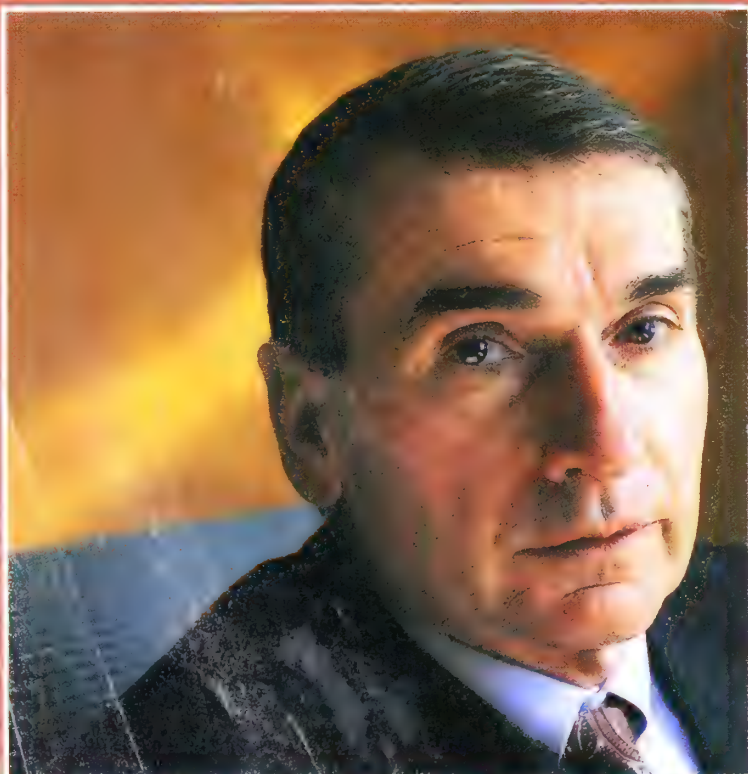
In any event, Steere's tenure at Pfizer will hardly be worry-free. One problem is Pfizer's potential liability for faulty mechanical heart valves made by its Shiley unit. Some 250 deaths since 1976 have been linked to ruptures in the valve. And if implant recipient Judy M. Khan wins a pending lawsuit against Pfizer for mental anguish, it could open up a floodgate to legal challenges. About 60,000 people worldwide have the implants. Indeed, during the next 10 years, Shearson Lehman Brothers Inc. estimates Pfizer could face anywhere from \$266 million to \$800 million in legal liabilities.

Another pressure: Pfizer must keep the cash spigot open for new drug development. Profits are strong, up 17.6% to

\$801.2 million, on a 13% increase in sales last year. But the company's financial resources are still dwarfed by those of Merck & Co. and Bristol-Myers Squibb Co. For instance, during the 1980s, Merck spent roughly 12% of its sales on R&D, vs. 8% at Pfizer. This year, however, Pfizer will spend about 10.5% of revenues on R&D.

A MAZE. Pfizer certainly has some hot drugs out on the market. One of the stars is Procardia XL, a cardiovascular drug whose sales could reach \$700 million this year. Another strong new entry is Diflucan, an antifungal medication used to treat AIDS and cancer patients which should do upwards of \$400 million in sales in 1991.

Pfizer is also trying to guide some promis-



New CEO Steere: "We were getting roasted by analysts when we were investing in R&D during the '80s"

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E5 Monoclonal antibody \$70

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DATA: MORGAN STANLEY & CO.

new drugs through the FDA's regulatory maze. This bunch, if approved, could fuel Pfizer's earnings growth all into the late 1990s. For instance, rvasc, a once-a-day cardiovascular, should contribute \$180 million in 1992 and up to \$900 million by 1995, says Alan Sebulsky, an analyst at Morgan Stanley & Co. Zolof, an antidepressant that will provide doctors with an alternative to Eli Lilly & Co.'s Prozac, could generate up to \$120 million in 1992.

Launching new drugs will make it possible for Pfizer to report the kind of double-digit earnings gains that have become common among pharmaceutical makers. Still, to join the upper echelon of drug companies, Pfizer may need to cut its low-return specialty chemicals business, which sells polydextrose and other ingredients to food makers. And some analysts believe Pfizer's specialty chemicals unit also should go.

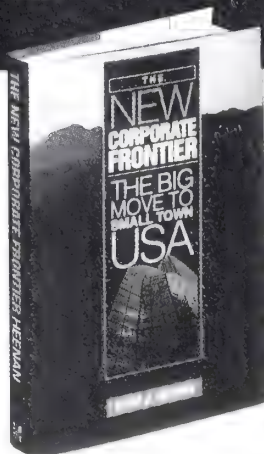
One financial measure tells the story: margins within those two businesses ran at 10% and 12%, respectively, compared with the 22% figure posted by Pfizer's health care operation. Steere isn't making any promises about divesting lagging units. But he offers a hint: "Given my 30 years in the pharmaceuticals business, my orientation is toward health care."

PIPELINE. Pfizer has already taken steps to boost profitability. In March, it sold its citric acid business—leaving the field in which the company began some 2 years ago. No doubt Steere could easily round up bidders for Pfizer's consumer products, such as Coty fragrances, Desitin and Ben-Gay ointments, and Visine eye drops. But he says that Pfizer wants to expand its consumer health care business by developing new products and making acquisitions. Pfizer's full pipeline has not gone unnoticed by Wall Street. Its stock was trading recently at 57%, up 27.5% since the beginning of the year. And it could go higher: Pfizer recently announced plans to buy back 10 million of its 330.4 million shares outstanding. Andrew S. Ofit, manager of the Fidelity Select Health Care Fund, expects Pfizer's earnings to increase 17.6% this year and 8% in 1992. "The one single negative on the horizon is the Shiley heart valve, but it's not enough to keep us from investing in the company," says Ofit. Although Pfizer's 1990 sales were substantially below those of industry giants such as Johnson & Johnson, Bristol-Myers Squibb, and Merck, Steere insists that Pfizer has no interest in merging with a deep-pocketed partner. Nothing wrong with wanting to cut your own size. Yet now the pressure is on Steere to make sure Pfizer's drug hit parade continues apace.

By Monica Roman in New York

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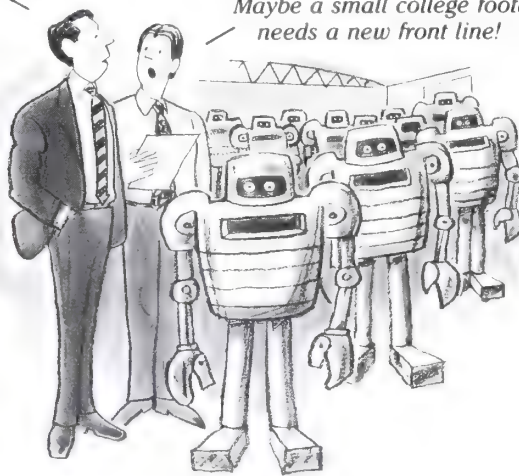
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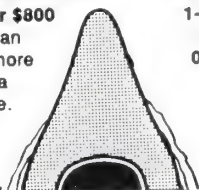
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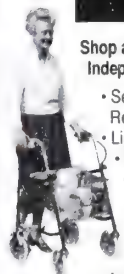
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EDITED BY JOAN WARNER

Health

THE SUN VS. YOUR SKIN: A SURVIVAL GUIDE

By now you've probably heard the warnings: The American Cancer Society expects that 600,000 new cases of skin cancer will be diagnosed this year, mostly caused by overexposure to the sun. One out of every six Americans will eventually de-

velop some form of skin cancer. For fair-skinned people, that rate increases to one in three. And in April, the Environmental Protection Agency announced that a shrinking ozone layer could lead to 200,000 Americans dying from skin cancer by 2050.

This is sobering news for those of us who slathered on baby oil, aimed reflectors at our faces, and blithely basked for hours. Will the indiscretions of our past necessarily doom us to skin cancer? The answer, say experts, is that with extra precaution now, maybe not. And the good

news is that over the past decade or so, major advances have been made both in spotting skin cancer early and treating it effectively.

DEEP DAMAGE. The sun's danger is invisible to us, existing in the form of ultraviolet light. The short rays that are responsible for a stinging sunburn and are thought to be the primary cause of photo-aging and skin cancer are called ultraviolet B (UVB). But research is revealing that its longer-wavelength cousin, UVA, may also cause damage. These longer rays produce a tan by reaching into the deeper layers of the skin and stimulating the production of melanin, a brown pigment.

There are three types of skin cancer, the most common type being basal cell carcinoma. Showing up mainly on the face, this type of skin cancer is slow-growing and rarely spreads to other parts of the body. Less common are squamous cell carcinomas, which grow faster than basal cell tumors and can sometimes spread to other parts of the body if not treated early. These rarely arise on normal skin but seem to grow on obviously sun-damaged skin. The deadliest and rarest of skin cancers, comprising just 5% of all skin cancers, is malignant melanoma. Although it's uncommon now, doctors say that melanoma has been increasing by 7% annually over the past decade and will kill 7,000 people this year.

Skin cancer most often occurs on areas exposed to the sun: the face, nose, ears, neck, and the back of the hands. It is slightly more common in men and is most likely to occur in middle age. People with light skin and light eyes are at greatest risk for skin



cancer; darker-skinned people have an extra degree of protection because they have a greater amount of melanin in their skin.

According to Dr. Perry Robins, a skin surgeon at New York University Medical Center and president of the Skin Cancer Foundation, the best defense against all types of skin cancer is vigilance. That's because the biggest gains against the disease have been made in spotting carcinomas early and treating them before there are complications. Even melanomas, if caught early, are curable. That means visiting a dermatologist to have all suspicious moles, dark patches, or long-lasting "pimples" checked.

SURGICAL STRIKE. Doctors usually treat early-stage skin cancer with surgery performed in the office under just a local anesthetic. Cancerous spots can also be burned, scraped, or frozen



MYTHS ABOUT SUNSCREENS

Perception	Reality
<i>It's O.K. to bask as long as you're wearing sunscreen</i>	Sunscreen protects you from some damage, but not all. Never bask at midday
<i>Many new products block UVA rays as well as UVB</i>	Only products containing the FDA-tested drug avobenzone Parsol block UVA
<i>Waterproof sunscreens protect you when you're swimming or sweating</i>	All sunscreens lose some power when diluted. It's safest to reapply
<i>Facial products are better for sensitive skin. Children need special sunscreens</i>	Facial, body, and children's sunscreens have mostly the same ingredients. Avoid PABA, a potential irritant, in all of them
<i>A sun-protection factor of 15 means it takes 15 times longer to tan. You can reapply the sunscreen after you've been out in the sun for more protection</i>	An SPF 15 does mean it takes 15 times as long to burn. But reapply before time is up. And do apply the stuff about 30 minutes before you catch some rays. It takes that much time for your skin to absorb the protective ingredients
<i>Expensive, designer-brand sunscreens contain moisturizers and protective ingredients that drugstore brands lack</i>	Many dermatologists say there's little difference. You're paying for packaging, fragrance, and extra chemicals

DATA: BW, CONSUMER REPORTS



f. A newer technique called Mohs micrographic surgery allows doctors to take a thin layer of the affected site, view it under a microscope to determine exactly where the cancer cells lie, and remove the cancer with great precision. According to Robins, who has trained about 300 surgeons in the technique, this surgery has higher cure rates and there is less scarring because only the cancerous tissue is removed.

If you don't have skin cancer, the burning question is how to stave it off. One area of progress has been in treating the precancerous spots called solar keratoses. These are scaly, flat, red or tan patches that form, usually on the face, back of hands or on bald pate. They aren't dangerous as such, but if neglected, can develop into squamous carcinomas. To treat these, doctors freeze or cut them off, or use harsh chemicals

such as 5-fluorouracil that are applied to the skin in the form of a cream. These chemicals cause the skin to redden and peel extensively—and may have other potentially serious side effects if applied incorrectly. But there are a few other promising treatments in the works, including a new drug called Actinex that in a

Melanoma is slowly on the rise: It will kill 7,000 people this year

A recent study reduced the number of solar keratoses by 71.4% in one month without the extreme skin irritation common to today's chemicals.

Retin-A, the acne-drug-turned-wrinkle-cream, may help reduce solar keratoses, but because it can take six months to a year to show re-

sults, "it has lost some of its glitter," says Robins. In the next couple of years, he adds, light-skinned people will probably be able to use a cream with a chemical that can safely stimulate the production of protective melanin before they are exposed to the sun.

IN THE SHADE. For those of us who worshiped the sun, believing it to be a benevolent deity, skin cancer is not inevitable. One dermatologist at Beth Israel Hospital in Boston says there is little evidence to support reports that a few bad sunburns as a child put an adult at serious risk for skin cancer. But the benefits of protection are undeniable. According to Robins, by age 55, the likelihood of getting skin cancer rises to 27,000 cases per 100,000 for those men who spent a lot of unprotected time out in the sun. But for those who avoided the sun, only 1,614 per 100,000 suffer the consequences.

That leads back to the advice doctors have been dispensing for the past decade: The best way to prevent skin cancer is to take refuge from the sun. One weapon is a good sunscreen that blocks out UVA as well as UVB and has a sun protection factor of at least 15 (box). Wearing a broad-brimmed hat and staying in the shade between 11 a.m. and 2 p.m. can also help. And remember that exposure to the sun just doesn't happen when you're stretched out on a towel. Long walks and volleyball games count, too.

And as you huddle under a beach umbrella and wipe the sting of sunscreen-laced sweat from your eyes, take solace in the fact that the deeply tanned surfer and his bronzed, bikini-clad companion next to you on the beach are anachronisms from the days when few people knew how dangerous the sun could be.

Naomi Freundlich

Getting Ahead

JUMP-STARTS FOR STALLED CAREERS

Recession has thrown a lot of employees off the fast track. And with the glut of forty-something baby boomers, more people are competing for fewer promotions. The result is an army of professionals stuck on a career plateau.

But there's help for the going-nowhere blues: career counseling. Using personality and aptitude tests, career counselors help clients assess their skills and character traits. These are combined into a vocational profile that is matched with job options. Next, counselors help target a field or job, based on how much risk clients can accept. The final step is a plan of

action to get a new job.

Career counselors charge \$50 to \$150 an hour, usually recommending 4 to 10 sessions. Some specialize in a field such as business or law. You can find them through the yellow pages, universities that have continuing education programs, or the National Association for Career Development (301 461-5574).

NETWORKING. Jump-starting a stalled career doesn't have to mean setting out on an unknown road. Right where you are, you can take on or create a special project to enhance your value to your company and vice-versa, says Michael Shahnasarian, a career counselor in Tampa. Or you can network with other departments to make a lateral move.

Take Bill Donahue, who felt stifled after eight years as a



computer programmer at Merrill Lynch. Career counseling at New York University's Continuing Education Center for Career & Life Planning bolstered his belief that he should be working with people, not machines. Talks with

the data processing staff led to a move into telecommunications, where the 32-year-old says he's happier.

Switching to a totally new field involves more risk. Here, counselors help clients determine how to transfer their skills. Fran Holzman used her experience when she was laid off as manager of an agency and got her current post managing industrial relations at a marketing firm. After her layoff, says Holzman, "fear was paralyzing me. But counseling [showed] me how I could apply the skills I already had."

To some, starting from scratch is worth the risk. Shahnasarian helped a doctor, who wanted a change after 17 years of teaching in medical school. He is now fulfilling a lifelong dream studying to become a tank captain. *Pam Blau*

Investors who march to a different drummer don't always call themselves contrarians. "It implies you're kind of a crackpot," says Robert Torray, whose Bethesda (Md.) firm manages \$1 billion. But Torray's strategy is the contrarian manifesto: "The best way to do well is to reverse the moves the rest of the people make."

Contrarians like to get into the market when the crowds are fleeing—thus depressing prices—and exit before the raging bulls slam into a wall. Veteran contrarians say the strategy is an automatic risk-reducer. By keeping away from what is fashionable, explains Jeremy Grantham of Grantham Mayo Van Otterloo, "you won't be buying horrendously overpriced art or real estate." Conversely, you're most likely to find real bargains among unpopular investments that high-profile analysts aren't following.

Even in times of high valuation, contrarians protect themselves by buying on the

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cheap (table). Vice-President Eric Hanson of Fraser Management Associates, which manages \$80 million and publishes *The Contrary Investor* newsletter, points to IBM as a current example. Negative press and disappointing earnings have recently pushed the stock price as low as 99¼ from a 12-month high of 139¼.

Similarly, Mark Millsap of Meridian Management loaded up on Chrysler bonds just after they were downgraded. The fiscal bad news in New England, says Lauren Eastwood of Gabriele, Hueglin & Cashman, has made 15-year munis issued by the Commonwealth of Massachusetts a high-yield bargain. She also sees a regional

rebound on the horizon.

So does Torray, who holds some controversial bank stocks, including Bank of Boston and Shawmut. Many contrarians agree that technology stocks, once considered a growth group, have joined the cyclical capital goods sector. Such battered issues as Digital Equipment says Millsap, are good long-term buys.

Market timing is not the contrarian's bag. Torray tells his clients to think in blocks of three to five years or more. So portfolio turnover is usually lower than that of an aggressive growth fund.

That's why contrarians consider themselves "value investors," identifying with the likes of Berkshire Hathaway's Warren Buffett or the Windsor Fund's John Neff, famous for their independent thinking and long-term success. Torray says that in the 1990s, more investors will follow fundamentals rather than fads. If he's right, he won't be a contrarian any more. *Joan Warner*

SOME CONTRARIAN PICKS

Investment	Status*	Rationale
IBM STOCK	Trading at 99¼, off 52-week high of 139¼	'What other shoes can drop at IBM?'
CHRYSLER BONDS	All senior debt downgraded to BB-	'It's a cyclical industry'
MASSACHUSETTS MUNIS	15-year munis yielding 7.5%, rated Bbb	'A default is highly unlikely'
BANK STOCKS	Moving up, but some are 50% off 52-week highs	'I still think they're cheap'
GOLD FUNDS	Many worth half what they were in 1987	'Gold is very oversold'

*As of June 17, 1991

DATA: BRIDGE INFORMATION SYSTEMS, BW

Autos

TOPLESS DRIVING FOR THE DOG DAYS AHEAD

Remember the first time you rode in a ragtop? The wind was in your hair, and you had the feeling of being the coolest driver on the road. Never mind that the air creaked, the roof leaked, and the rear plastic window yellowed and cracked.

Well, they're making convertibles better these days. But they will probably never match coupes in structural integrity or convenience. After all, they're missing a steel roof. Rear seats are narrow-

verted from a coupe straight off the assembly line, expect to pay a \$4,000 or \$5,000 premium over a standard model.

Careful shopping can lessen the annoyances.

The key is a rigorous test-drive. Do the windshield frame and doors rattle when you drive over a rutted road? Do you have to be Arnold Schwarzenegger to close a



THE CHEAPEST "ONE-BUTTON TOP" IS INFINITI'S \$31,000 M30. OTHER GOOD CHOICES AT SIMILAR PRICES: MAZDA'S RX-7, BMW'S 318i, AND SAAB'S 900S



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, and trunks are smaller, designed to accommodate the rack, or roof mechanism. Then, there's the matter of raising and stowing the top and fitting the boot (the cover that hides the top and stack when the top's down). And then was the last time you washed your car by hand instead of by car wash?

DREAM BOATS. The romance of convertibles is enough to win people, and carmakers know it. There are more than 100 factory-approved nameplates on the U.S. market—virtually all converted by outside companies—more than at any other time. They range from the under-\$10,000 Geo Metro to the more than \$225,000 Rolls-Royce Corniche. If the car has been con-

verted with a "one-hand" manual top? Is there a rigid boot that quickly drops into place, or a Velcro affair that takes 10 minutes to settle?

Tops among available ragtops has got to be the Mercedes-Benz 500SL, which has the most elegant roof mechanism ever designed. Pressing a single button in the \$90,000 two-seater unlatches the top from the header, lowers it, stores it under a hard boot, and rolls down the windows. And this convertible is the only one with a true roll bar. It pops up automatically in a crash, or you can en-

gage it with a dashboard switch. A winter hardtop is standard. Find out if your dealer will store it over the summer and reinstall it in the fall—some do it for free.

The Porsche Carrera, at \$72,000 and up, aims for the same effect but requires you to unzip the plastic rear window before the top comes down and to install a canvas boot afterward. The only cheaper "one-button top" is on the new \$31,000 Infiniti M30. Along with the \$28,000 Mazda RX-7, these are among the soundest convertibles. Other good choices for around the same price are the BMW 318i and the Saab 900S.

More accessible, and thus popular, are the \$14,000-to-\$20,000 ragtops. Among them is the wildly popular Mazda Miata, available this season in a \$19,000 Special Edition in British Racing Green, with a sumptuous beige-leather interior—an improvement over the \$14,000 base model's black fabric. Don't be misled by the

Australian-built Miata pretender, the Mercury Capri. As *Consumer Reports* puts it: "A sports car should be fun to drive—and our test drivers all agree that the Capri isn't."

SHIVERS. Among Detroit's entries, America's favorite convertible is the \$16,000 Chrysler Le Baron. Its styling is gorgeous and, with the top up, it's one of the quietest ragtops. But with the top down, it fails at freeway speeds: It's buffeted by noisy wind and, unlike most other convertibles, its heater can't keep up. The Le Baron and the next most popular, the Ford Mustang, sport power tops and glass rear windows. If you want muscle, try the Pontiac Firebird. Or double up to a \$40,000 Corvette, whose sound system automatically cranks up the volume as you accelerate.

So what if the boot is a pain? What's a leak, when it never rains in Southern California? Just turn up the radio and cruise. *Larry Armstrong*

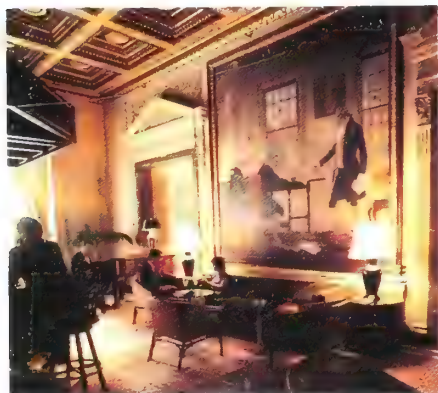


AMONG DETROIT'S ENTRIES, THE \$16,000 CHRYSLER LE BARON IS AMERICA'S FAVORITE. WITH THE TOP UP, IT'S ONE OF THE QUIETEST CONVERTIBLES AROUND

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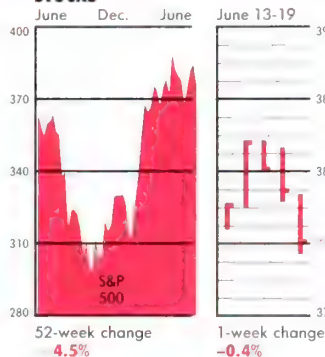
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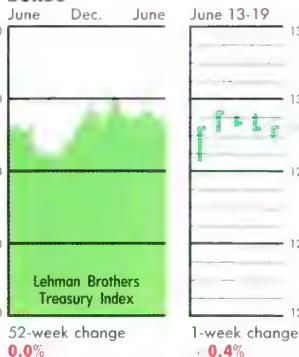
COMMENTARY

Markets find it hard to live in prosperity. As the numbers continued to signal economic recovery, the Dow industrials once again backed off from 3000. The line on June 19 was particularly severe, with the Dow shedding more than 31 points. New York seemed to take its cue from Tokyo where stocks tumbled almost 200 points, or 2.8%, overnight in the aftermath of stronger-than-expected first-quarter economic growth. Still, the technical factors point to an up market.

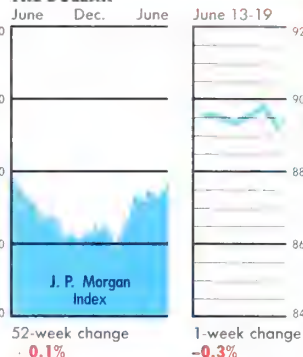
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS	Latest	% change Week	% change 52-week
DOW JONES INDUSTRIALS	2955.5	-0.2	2.1
COMPANIES (Russell 1000)	196.0	-0.4	4.9
ALL COMPANIES (Russell 2000)	172.9	-1.0	2.8
COMPANIES (Russell 3000)	208.5	-0.4	4.8

FOREIGN STOCKS	Latest	% change (local currency) Week	% change (local currency) 52-week
LONDON (FINANCIAL TIMES 100)	2484.7	-1.4	4.8
TOYO (NIKKEI INDEX)	23,996.8	-2.0	-25.2
TOKYO (TSE COMPOSITE)	3529.5	-0.8	0.0

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.7%	5.7%	8.0%
30-YEAR TREASURY BOND YIELD	8.5%	8.5%	8.5%
S&P 500 DIVIDEND YIELD	3.2%	3.2%	3.2%
S&P 500 PRICE/EARNINGS RATIO	17.8	17.9	16.5

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 26-week moving average	363.1	361.2	Positive
Stocks above 26-week moving average	68.6%	73.7%	Neutral
Speculative sentiment: Put/call ratio	0.49	0.43	Positive
Insider sentiment: Vickers sell/buy ratio	1.95	1.91	Positive

INDUSTRY GROUPS

4-WEEK LEADERS

	% change 4-week	% change 52-week
MACHINE TOOLS	19.2	-35.2
PAPER CONTAINERS	18.3	17.7
AUTOMOBILES	17.9	-15.3
AFTERMARKET AUTO PARTS	14.4	3.1
HAIRDWARE AND TOOLS	13.5	0.4

4-WEEK LAGGARDS

	% change 4-week	% change 52-week
HOMEBUILDING	-7.8	4.8
PUBLISHING	-5.9	-2.9
HEALTH CARE SERVICES	-5.5	71.6
HOSPITAL MANAGEMENT	-5.3	10.2
RESTAURANTS	-4.9	-5.5

Strongest stock in group

	% change 4-week	% change 52-week	Price
CROSS & TRECKER	86.4	-43.8	51/8
STONE CONTAINER	33.6	19.9	233/8
GENERAL MOTORS	20.0	-13.4	43 1/2
GOODYEAR TIRE & RUBBER	43.2	-1.8	34
BLACK & DECKER	26.8	-3.9	153/8

Weakest stock in group

	% change 4-week	% change 52-week	Price
PHM	-23.5	53.0	125/8
TIME WARNER	-20.8	-12.1	935/8
MANOR CARE	-11.6	39.4	18 1/8
HUMANA	-7.9	2.8	463/8
McDONALD'S	-5.5	-8.8	32 1/4

MUTUAL FUNDS

LEADERS

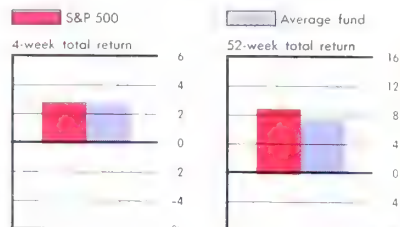
	4-week total return	%
STRATEGIC INVESTMENTS	22.5	
STRATEGIC SILVER	11.9	
FINANCIAL STRATEGIC GOLD	10.2	

	52-week total return	%
IDEALITY SELECT BIOTECHNOLOGY	59.9	
IDEALITY SELECT HEALTH CARE	53.3	
IDEALITY SELECT MEDICAL DELIVERY	52.7	

LAGGARDS

	4-week total return	%
EQUITY STRATEGIES	-7.0	
DFA UNITED KINGDOM SMALL COMPANY	-6.0	
DR EUROPEAN EQUITY	-4.9	

	52-week total return	%
BULL & BEAR SPECIAL EQUITIES	-42.3	
STEADMAN OCEANOGRAPHIC TECHNOLOGY	-40.4	
STEADMAN AMERICAN INDUSTRY	-33.9	



RELATIVE PORTFOLIOS

Amounts represent the present value of \$10,000 invested one year in each portfolio.

Percentages indicate daily total returns.

Gold
\$10,672
-0.36%

U. S. stocks
\$10,647
-0.65%

Treasury bonds
\$10,641
-0.51%

Money market fund
\$10,619
+0.11%

Foreign stocks
\$9,354
-0.22%

Data on this page are as of market close Wednesday, June 19, 1991, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of market close.

June 18. Mutual fund returns are as of June 14. Relative portfolios are valued as of June 18. A more detailed explanation of this page is available on request.

CASH ON DELIVERY OF SOVIET REFORMS

Boris N. Yeltsin's election as President of the Russian Republic promises to give a powerful new impulse to Soviet economic and political reforms. Yeltsin won on a platform calling for drastic steps toward a market economy. The resulting popular mandate in the giant Russian Republic seems sure to pull other Soviet republics in the same direction. And for Soviet President Mikhail Gorbachev, the example of Russia should tilt the political balance toward his goal of *perestroika*, or restructuring, after six years of lurching between reform and the status quo.

The brighter prospects for a market economy sharpen the choices for Western leaders, who have asked Gorbachev to meet with them in London following the July 15-17 economic summit. Gorbachev is expected to ask for financial help for reforms. Certainly, the U.S. and its allies aren't going to pledge money for mere promises. But it is surely in the West's interest to encourage the Soviet Union to continue its transition from a dictatorship run by a secretive clique in the Kremlin toward an open society in which economic and political power flows both to and from the grass roots.

Western leaders should consider giving aid for specific Soviet reform measures. A hard-currency-stabilization fund, for example, would smooth a difficult transition to ruble convertibility, while financing for temporary imports of goods would dampen inflation when prices are freed. Any such help must also be tied to further steps toward democracy, such as Gorbachev's promise to hold free elections for the Soviet presidency and parliament. That pledge is part of the Apr. 23 pact by nine republics and the Kremlin to negotiate a new treaty to reshape relations among them.

What seems likely to emerge is a federal system in place of the highly centralized Soviet Union. Western help must strengthen the role of the republics and private enterprise, not merely shore up centralized controls. Europe and Japan, which stand to benefit as much as the U.S. from such a transformation, have to put up their full share of any assistance. And after so many false starts, it can only be dispensed on a pay-as-you-go basis: no reform, no aid.

THE FED'S BEST MOVE IS NO MOVE

The Federal Reserve has often been condemned for sitting on its hands during critical junctures in the business cycle. With the data now showing that recession is giving way to a recovery that could be surprisingly strong and durable (page 48), this is one of those key moments. The question now is whether the Fed needs to do more to maximize the chances that the U.S. economy will flourish. The answer is no. The Fed is doing exactly what it should be doing—zilch.

Tweaking monetary policy in either direction right now

could hurt the nascent recovery. The bond market has already pushed up long-term interest rates for fear that an upturn will generate inflation. Therefore, the Fed dares not cut short-term interest rates any more for recovery insurance, because bond traders would push up long rates even further. That would threaten the budding upturns in such credit-dependent areas as housing, autos, and other big-ticket consumer goods.

On the other side, the Fed cannot consider tightening until the strength of the recovery becomes clearer. The long-term goal is to wring inflation out of the economy, but clamping down on credit too early in the recovery would run the risk of killing it off altogether.

Alan Greenspan has already said—as clearly as any Fed chairman is going to say it—that the recession is probably over. He has even raised the possibility that the recovery could be surprisingly strong. But he has been wary, correctly, of saying that the recovery has begun, citing the ongoing problems in real estate and the hesitancy of banks to lend. Until a clearer picture of the economy emerges, the Fed is right to sit tight.

PETE WILSON SHOULD KEEP HIS HANDS OFF CALPERS

In the past few years, the California Public Employees Retirement System has become the prototypical activist institutional shareholder. With \$65 billion in assets, CalPERS is unable to move in and out of its holdings easily. So to get a good return, the fund must do what it can to make sure the companies in its portfolio do well.

CalPERS has pioneered several kinds of shareholder resolutions and paid outside consultants to analyze companies and to provide expertise in areas, such as compensation, that are beyond its ken. Although it has jawboned instead of making war, some corporate executives still see CalPERS and other activist institutional investors as antagonists—but the more enlightened ones do not. As one source close to the Business Roundtable puts it: "Management has come light-years closer to this. There's a very healthy tension between members and institutional investors; it's a constructive dialogue."

That's why California Governor Pete Wilson's broadside at CalPERS—whatever his reasons—is wrongheaded (page 29). Wilson is attempting to control CalPERS' board and recapture a couple of billion dollars' worth of the fund's surplus to ease the state's \$14 billion deficit. But the fund's corporate-governance activities should be encouraged, not curtailed. Management needs to be accountable to shareholders. And CalPERS should be held accountable primarily to its current and future pension participants, whose representatives now number 6 on a 13-member board—not to political appointees, whose motives may conflict and who have no stake in the fund's success. Finally, CalPERS can't be expected, because of its success, to balance the state's budget—though it may have to stop looking to the state to make up its funds when it does poorly. When it comes to pensions, Wilson, unlike CalPERS, is setting a bad example for other state and local governments that are stretched for funds.

BusinessWeek



LY 8, 1991

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RACE **IN THE** WORKPLACE

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NOT ENOUGH: LIBERTY NATIONAL BANK IN LOUISVILLE HAD A SOLID MINORITY-HIRING RECORD—AND STILL RAN AFOUL OF FEDERAL RULES

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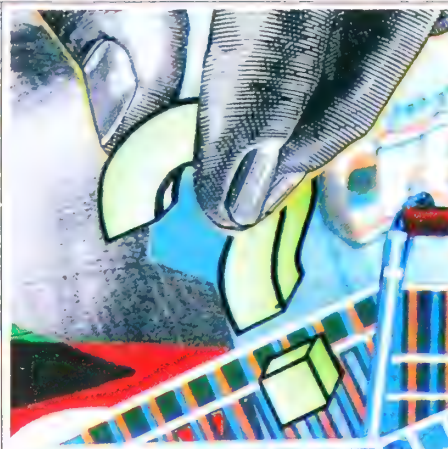
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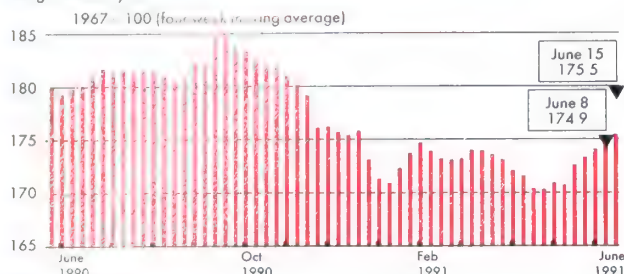
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BusinessWeek Index

PRODUCTION

Change from last week: 0.3%
Change from last year: -2.6%

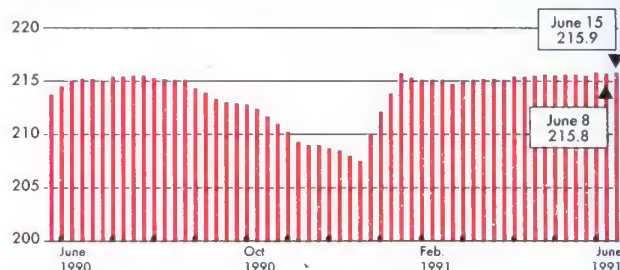


The production index was up sharply for the week ended June 15. On a seasonally adjusted basis, output of autos, steel, and coal rose strongly, and truck, electric power, crude-oil refining, rail-freight traffic, and lumber production increased as well. Paper output fell, and paperboard production was unchanged. Prior to calculation of the four-week moving average, the index jumped to 177.6, from 174.4 in the previous week.

BW production index copyright 1991 by McGraw-Hill Inc.

LEADING

Change from last week: 0.0%
Change from last year: 0.3%



The leading index was little changed during the week ended June 15. Sharply lower stock prices and higher long-term bond yields offset the positive signs of higher growth rates for real estate loans and M2, plus a smaller rate of decline in the prices of industrial materials. Data on business failures were unavailable for the week. Before calculation of the four-week moving average, the index rose slightly to 215.9, from 215.5 in the week before.

Leading index copyright 1991 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (6/22) thous. of net tons	1,556	1,630#	-17.7
AUTOS (6/22) units	118,558	118,390r#	-20.9
TRUCKS (6/22) units	82,825	78,977r#	-10.4
ELECTRIC POWER (6/22) millions of kilowatt-hours	62,839	60,055#	1.0
CRUDE-OIL REFINING (6/22) thous. of bbl./day	14,011	14,001#	3.9
COAL (6/15) thous. of net tons	19,686#	19,097	-1.7
PAPERBOARD (6/15) thous. of tons	765.4#	761.0r	2.4
PAPER (6/15) thous. of tons	727.0#	736.0r	-0.8
LUMBER (6/15) millions of ft.	546.2#	537.3	9.3
RAIL FREIGHT (6/15) billions of ton-miles	19.6#	19.0	-3.9

Sources: American Iron & Steel Inst., Ward's Automotive Reports, Edison Electric Inst., American Petroleum Inst., Energy Dept., American Paper Inst., WWPA, SFPA, Association of American Railroads.

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (6/26)	138	140	152
GERMAN MARK (6/26)	1.78	1.79	1.67
BRITISH POUND (6/26)	1.64	1.63	1.74
FRENCH FRANC (6/26)	6.06	6.10	5.61
CANADIAN DOLLAR (6/26)	1.14	1.14	1.17
SWISS FRANC (6/26)	1.54	1.54	1.41
MEXICAN PESO (6/26) ¹	3,007	3,002	2,858

Sources: Major New York banks. Currencies expressed in units per U. S. dollar, except for British pound expressed in dollars.

PRICES

	Latest week	Week ago	% Change year ago
GOLD (6/26) \$/troy oz.	366.100	367.400	4.4
STEEL SCRAP (6/25) #1 heavy, \$/ton	89.00	89.00	-22.3
FOODSTUFFS (6/24) index, 1967=100	199.2	199.9	-12.1
COPPER (6/22) c/lb.	103.4	103.8	-12.0
ALUMINUM (6/22) c/lb.	60.5	58.5	-17.5
IRON (6/22) #2 hard, \$/bu.	2.97	3.02	-13.9
IRON (6/22) strict low middling 1-1/16 in., c/lb.	79.49	79.31	3.0

Sources: London Wed. final setting, Chicago mkt., Commodity Research Bureau, Metals Week, Chicago, Memphis mkt.

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (6/21) S&P 500	377.39	375.25	5.4
CORPORATE BOND YIELD, Aaa (6/21)	9.05%	9.01%	-2.3
INDUSTRIAL MATERIALS PRICES (6/21)	98.9	98.4	-3.7
BUSINESS FAILURES (6/14)	NA	359	NA
REAL ESTATE LOANS (6/12) billions	\$405.3	\$404.7r	7.5
MONEY SUPPLY, M2 (6/10) billions	\$3,399.1	3,386.7r	4.0
INITIAL CLAIMS, UNEMPLOYMENT (6/8) thous.	448	401	25.8

Sources: Standard & Poors, Moodys, Journal of Commerce (index: 1980=100), Dun & Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. CIBCR seasonally adjusts data on business failures and real estate loans.

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
ORDERS FOR DURABLE GOODS: MFG. (May) billions\$	121.5	116.1r	-7.2
HOUSING STARTS (May) annual rate, thous.	982	981r	-18.7
RETAIL SALES (May) billions	\$152.5	\$150.9r	2.5
REAL GROSS WEEKLY PAY (May)	\$256.32	\$253.83r	-5.1

Sources: Commerce Dept, Census Bureau, BLS

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (6/10)	\$856.5	\$850.6	6.1
BANKS' BUSINESS LOANS (6/12)	309.5	312.0	-5.9
FREE RESERVES (6/12)	440r	879r	NM
NONFINANCIAL COMMERCIAL PAPER (6/12)	148.4	148.9	-0.1

Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed for a two-week period in millions).

MONEY MARKET RATES

	Latest week	Week ago	Year ago
FEDERAL FUNDS (6/25)	5.90%	5.82%	8.28%
PRIME (6/26)	8.50	8.50	10.00
COMMERCIAL PAPER 3-MONTH (6/25)	6.11	6.11	8.25
CERTIFICATES OF DEPOSIT 3-MONTH (6/26)	6.04	6.04	8.27
EURODOLLAR 3-MONTH (6/22)	6.05	6.13	8.23

Sources: Federal Reserve Board, First Boston

production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. ¹Products Assn. ²Southern Forest Products Assn. ³Free market value NA=Not available r=revised NM=Not meaningful

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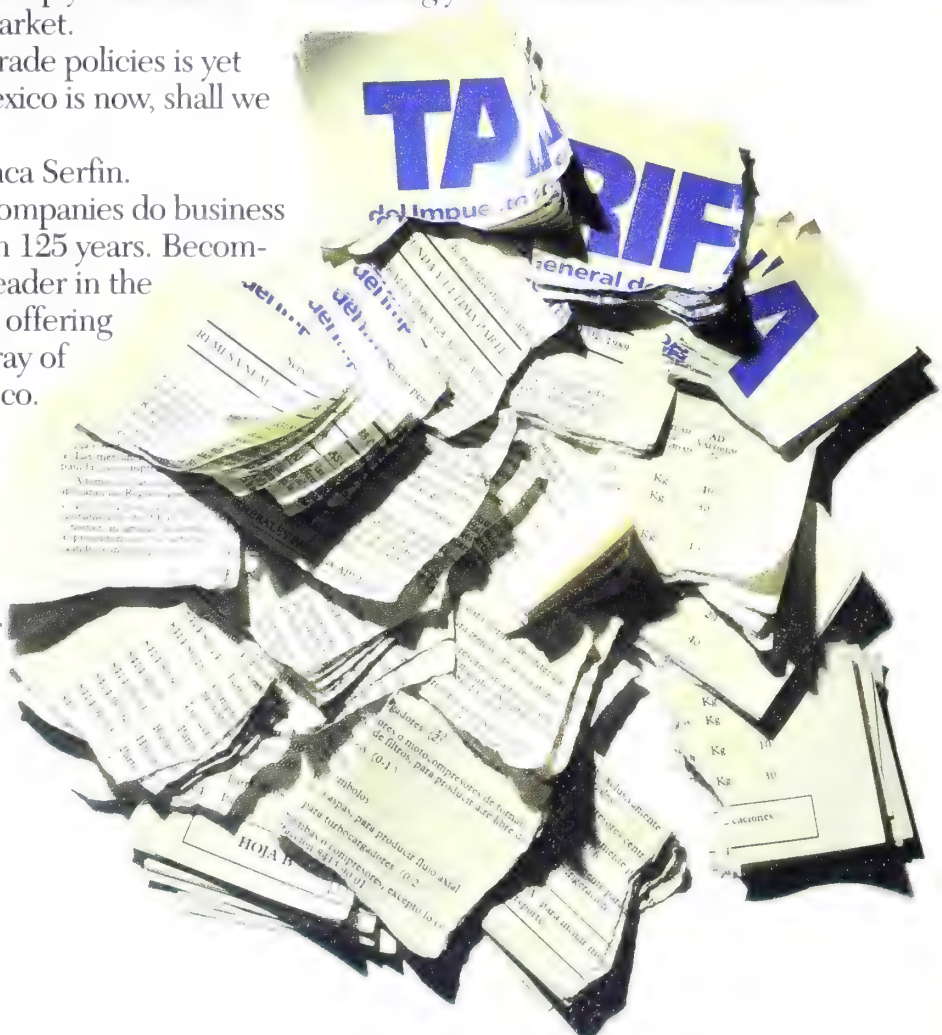
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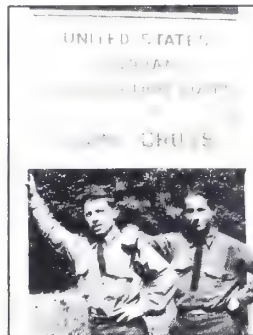
There are 130 of them. Of all ethnic backgrounds. From all over San Francisco.

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It's all in a day's work. The Civilian Conservation Corps proved it



50 years ago, helping young people to help themselves and their communities beat the Depression.

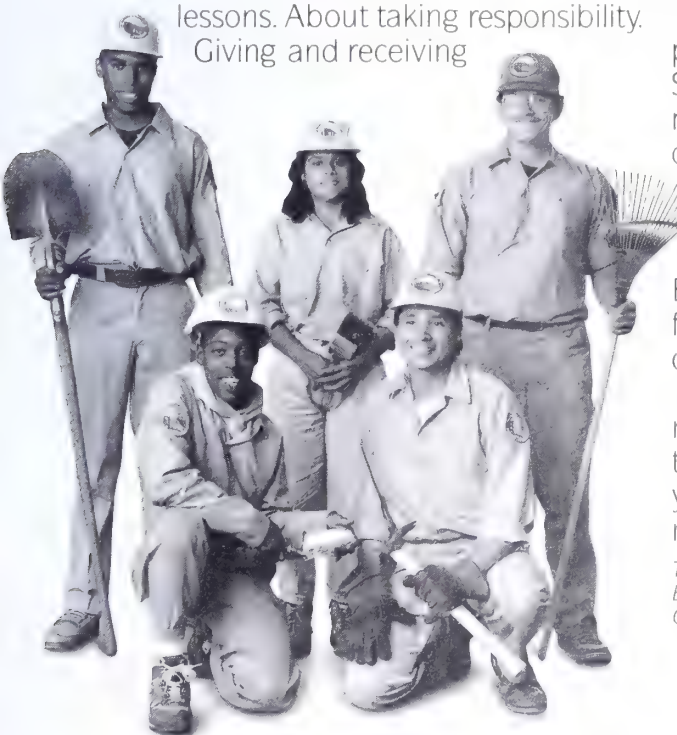
Today, the SFCC addresses similar problems that weigh heavily on the minds of San Francisco businesspeople. Unemployment. Declining city infrastructure. And, developing a strong work ethic among young people.

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Readers Report

al and cross-level group processes that encourage commitment (rather than tension) and cooperative, creative planning, building, and selling?

Changing people's minds about shifts in personal power and communication is the major challenge for the U.S. human system. IBM is fortunate to have its technology be its model.

Ann R. Thomas
Ann Arbor, Mich.

Our experience with IBM marketing reps? Instead of asking us what we need or want, they tell us what we should do with what IBM has already dictated, something that does not make sense for us. And they have no flexibility to meet our needs.

Michael J. Pochan, President
LeaseTek
Pittsburgh

As a two-week office temp at IBM's San Francisco office last summer, I could not believe the number of hours and dollars being wasted on a presentation that would be given to John Akers that would merely report IBM's performance in that region. For two weeks, 50 people labored 14 hours a day on an

elaborate presentation with graphics and multimedia, spending thousands of dollars—all so that a few middle managers would impress Akers. With such mindless politicking going on, it is no surprise that IBM has lost touch with its customers and the market.

Michael M. De Jesus
Chicago

While you mention the amount of money IBM invests in research and development, I do not believe that you attached sufficient importance to how that can bring about such significant announcements as introducing the IBM System/360. Second, you failed to highlight a real plus for IBM in that, for the past several years, it has initiated numerous acquisitions and joint ventures that bring a great deal of breadth to its customer base. These are just two of the positive aspects of IBM's future.

J. Gerald Simmons
New York

Today's computer customers need solutions—and care less about technology. Solutions contribute to higher productivity and profits and get attention from all management levels. Selling so-

lutions requires customization and extensive knowledge of the customer-business environment, a lengthy, tedious and expensive process. IBM has yet to master selling customized solutions.

M. Russ Adamian
Bridgewater, N.J.

Your treatment John Akers can only make one ask "Where are the emperor's clothes?" Akers, who has held the CEO position for "six disappointing years," has slashed 47,000 workers from the payroll and has watched profitability and market share erode while he lays blame on everyone except management. One must ask if the board is culpable in its 185% increase of his pay and bonus.

I was surprised that several astute IBM employees questioned management's role in IBM's decline, but none of your "six gurus" had nerve enough to address the obvious.

Tom Rush
Memphis

Letters to the Editor should be sent to Readers Report, Business Week, 1221 Avenue of the Americas, New York, N.Y. 10020 Fax: (212) 512-4464, Telex: 12-7960, Intl. 4998204. All letters must include an address and daytime and evening telephone numbers. We reserve the right to edit letters for clarity and space.

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THE FREEDOM OF ONE.

UNDER THE INFLUENCE: THE UNAUTHORIZED STORY OF THE ANHEUSER-BUSCH DYNASTY

By Peter Hernon and Terry Ganey • Simon & Schuster • 461pp • \$24.95

THE KINGS OF BEER, FROTH AND ALL

During the 1860s, Eberhard Anheuser and his son-in-law Adolphus Busch, partners in a small St. Louis brewery, were having trouble persuading consumers to buy their beer. So, they tried a new approach. They began paying taverns to promote the brew. They even bought some taverns, which began to serve their beer exclusively.

In the years ahead, such tactics served the partners well. The little brewery grew into Anheuser-Busch Cos., the world's biggest beermaker, which dominates its industry in a way matched by few, if any, other consumer-product concerns. Thanks largely to its best-selling Budweiser brand, the company produces 44% of the nation's beer. Miller Brewing Co. is a distant second, with 22%. A-B's share seems to grow inexorably, while those of rivals fade.

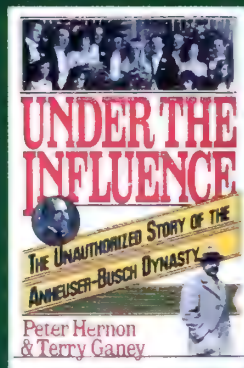
A-B makes good beer. But the main reason for its success, according to *Under the Influence*, the first book about the company, is that the beer giant is tougher, rougher, and shrewder than its competition. Its marketing tactics sometimes resemble military assaults. When Miller threatened its lead during the 1970s, for instance, A-B launched a campaign consisting of 10,000 separate sales-promotion programs that divided the country into not only cities and neighborhoods but also individual streets and bars. A-B has been accused of such hardball tactics as illegally monopolizing beer sales at ballparks, racetracks, and arenas. Retailers would agree to sell A-B beers exclusively, and, in return, the company allegedly would give them fixtures, advertising services, and other inducements. While the company has denied some allegations, in other cases it has admitted such tactics, claiming they were used "for competitive reasons."

As remarkable as A-B's hegemony over the industry is the family that has run the company since the days of Adolphus Busch, who eventually pushed out the Anheusers. In this gossipy, fact-

filled account by Peter Hernon and Terry Ganey, journalists with the *St. Louis Post-Dispatch*, the Busches, a five-generation dynasty without parallel in American business, are the chief focus.

Bloodlines in family corporations often thin out as control passes to successive generations, but the Busches just seem to get tougher. While beer may not run in their veins, the company often points out that August A. Busch III, the CEO, and August A. Busch IV, his heir apparent, were fed small amounts of beer shortly after they were born.

A tabloid-speak
saga of sex scandals,
Busch family feuds,
and a closetful of
other skeletons



August III, the book says, is "as capable a corporate head as this country ever produced." Like his forebears, he is also fiercely competitive. He took over in 1975 by deposing his father, August A. "Gussie" Busch Jr. A family member cited in the book says that August III went to all the board members, many of whom had business ties with A-B, and said: "If you want to continue doing business with the brewery, you'll vote for me against my father."

Much of *Under the Influence* is devoted to the Busches' extracurricular activities—a Dallas-size saga of sex scandals, family feuds, and a closetful of other skeletons. In overheated tabloid-speak, Hernon and Ganey describe how the same affinities and peccadilloes have plagued each generation of Busch men: a taste for guns, booze, glamorous women, and fast cars. The family history includes an astounding number of auto

accidents, several of them fatal and involving alcohol.

The Busches also flaunt extravagance. Gussie Busch assembled a menagerie of hundreds of exotic animals from around the world. He even built an artificial mountain for a herd of mountain goats. And the family loves elaborate wedding and funerals. In 1918, shortly after the funeral procession began for Adolphus Busch, all power in St. Louis was shut off for five minutes so that the entourage could observe a moment of silence. His body was interred in a huge mausoleum on which is emblazoned *Veni Vidi, Vici*.

Unfortunately, the authors fall prey to their own sort of extravagance. They seem eager to share every morsel gathered during their two years of sleuthing. Fact is piled upon fact, often with little perspective or analysis.

And for the business reader, at least the authors' priorities are skewed. They devote 14 pages to how Gussie's son Peter accidentally shot and killed a friend. Yet they dismiss in five pages the company's most embarrassing scandal, an extensive kickback scheme that came to light in 1988. Top Anheuser-Busch executives were convicted of routinely accepting costly gifts from advertising agencies and other companies in exchange for business. One defendant later wrote the authors that he had "witnessed incredible greed and corruption at the highest levels of the company. I saw il-

legal activities and I saw flagrant personal misuse of corporate and thus shareholder funds." These are arresting allegations, but the authors apparently did not follow up on them.

The book also says surprisingly little about the multifarious ways in which the company has maintained its primacy in beer. It describes several times how family members and friends of the company often are awarded lucrative distributorships, but it doesn't even mention how Anheuser-Busch, in the view of some rivals, uses its powerful network of exclusive distributors to squeeze out competitors.

Still, taken as real-life soap opera, *Under the Influence* makes a lively beach read. You might bring along a cold six-pack.

BY CHRIS WELLES

Senior Writer Chris Welles generally orders club soda.



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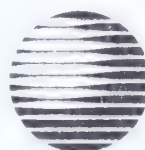
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GO AHEAD. GIVE GORBY MONEY —AND KILL SOVIET REFORM

BY PAUL CRAIG ROBERTS



U.S. aid now would only strengthen the established bureaucracy and snuff out the vital, unofficial market economy that has started to blossom from below

The debate over aid to the Soviet Union took a new turn when Mikhail Gorbachev said in his Nobel peace prize acceptance speech that peaceful co-existence could be threatened if Western nations failed to help ward off instability and chaos in his country. Senator Bill Bradley (D-N.J.), an opponent of large-scale aid, responded sharply: "It is an attempt at a new form of nuclear blackmail: 'Give us money or we won't be able to control our nuclear weapons.'"

Senator Bradley may be onto something. Western aid would have nowhere to go except into existing Soviet institutions—thus strengthening the very problems that must be overcome. The subsidies would give the Kremlin a new lease on life and would prove difficult to terminate should reform falter. Rather than face the consequences of cutting off aid, Western politicians would be likely to lean toward arguments such as "\$30 billion a year wasn't enough to do the job, but \$50 billion would suffice." The temporary aid could easily evolve into a permanent entitlement in an effort to ensure cooperation by gluing the Soviet Union together with our money.

The aid plan recently in the news was cooked up by Soviet reformer Grigory Yavlinsky with input from some Harvard University professors. It envisages the purchase of a democratic, market-oriented Soviet Union with Western aid. Although eager for the money, the Soviet government has denounced the plan because it foresees interference in its internal affairs.

Most reformers don't like it, either. In an address to the Russian parliament earlier this year, Boris N. Yeltsin, Russia's recently elected President, stated that he believes Western aid is used by the Kremlin as an agent of political control, and the plan was denounced by members of Yeltsin's recent delegation to Washington. Moscow Mayor Gavril Popov, a reform leader, has also expressed opposition: "The aid package will kill the democratic process. By providing the Communist establishment with monetary salvation, all incentive for real reform will be lost."

INITIATIVE. As I noted in an earlier column (BW—May 13), an unofficial reform process is already under way. Privatization is occurring in fact if not in law, as plant managers and political bosses assume property rights by acting as if they were owners. Bypassing central bureaucracies, managers are relying more on their own initiative to organize production, thus creating market relationships in place of official supply channels.

Reform of the Soviet economy is likely to proceed largely along these lines, with people

turning their backs on the old order, seizing opportunities, and creating new ones. There is no possibility that a grand reform plan could be superimposed on this process without causing opposition by cutting across the unofficial relationships and rights already in place.

The idea of a "grand bargain" to remake the Soviet Union reflects the hubris of the modern academic and political mind. Neither Cambridge nor Washington can envisage people being allowed to sort things out for themselves. Perhaps the best way for Soviet and republic authorities to advance the reform process is by legalizing private ownership and the informal economy—and not looking too closely at the process by which property is already becoming private.

RENEWED FOCUS. By focusing on the timing and amount of aid necessary to prevent Soviet economic catastrophe and political instability, we are thinking about the problem in the wrong way. Instead, we should focus on leading the Soviets to economic liberty. If the devastated communist countries are to revive, it will be with our ideas. This will be a greater challenge to us than providing aid because it will force us to reaffirm our own ideals.

The Soviet government will continue to sink until it learns to trust its own people and look to their energies and initiatives as its greatest economic resource. No amount of Western aid can compensate for rules of economic behavior that keep people from producing goods and services that are valued by markets, or for the absence of institutions that can effectively use human, financial, and physical capital.

It is naive to assume that Western strings on aid would guarantee successful reforms. Advice from the World Bank or the International Monetary Fund is unlikely to be any more successful in the Soviet Union than it has been in Latin America and Africa. If the IMF's conditions can't be successfully imposed on those governments, they would amount to little more than empty talk in the Soviet Union.

President Bush's choice of Democrat Robert S. Strauss as our new Soviet ambassador suggests that he is leaning toward aid. Since polls show that Americans are opposed, Bush has moved to disarm Democrats by making his Soviet policy bipartisan. But before the President jumps into a quagmire larger than the Arab-Israeli conflict, he might ponder how much money we have thrown, without success, at our own, much smaller, domestic problems. It would be unforgivable if Bush, in an effort to help his friend Gorby, ends up feeding the old Kremlin bureaucracy with new U.S. tax dollars.

PAUL CRAIG ROBERTS IS CHAIRMAN OF THE INSTITUTE FOR POLITICAL ECONOMY IN WASHINGTON



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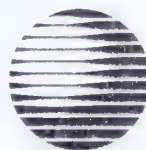
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BY GENE KORETZ

RECOVERY? DON'T TELL THAT TO METALS PRODUCERS

As economists scan the horizon for signs of economic recovery, one leading indicator is conspicuous by its lackluster performance. Sensitive materials prices, which normally perk up as business starts to turn around, have been falling steadily since the third quarter of last year. "If we're on the verge of a vigorous upturn," says economist Christopher Plummer of economic consultants WEFA Group Inc., "it's certainly not apparent in industrial commodity prices."

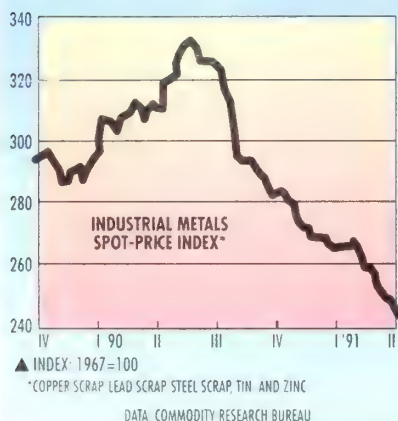
Metals prices, which tend to respond to shifts in industrial production and to

ing recessions producers tend to build up large inventories that take some time to work off. Moreover, he notes that economic sluggishness overseas and a strong dollar are still exerting downward pressure on U.S. metals prices.

Metals economist Fred Demler of PaineWebber Inc., points out, however, that whereas world metals inventories doubled or tripled during earlier U.S. recessions, they are up only 20% to 30% over the past year. Because stocks are being controlled more intensively than in past business cycles, he thinks metals markets may already be bottoming out and could post significant price appreciation in the months ahead.

According to economists at WEFA Group, the critical issue is the strength of the upturn. "Because we expect an anemic recovery," says WEFA's Frantz Price, "we think prices of metals and other industrial materials could remain weak until the fourth quarter."

METALS PRICES CONTINUE TO SLIDE



pickups in such bellwether industries as autos and housing, have been especially weak (chart). Copper prices have fallen from \$1.35 a pound about a year ago to \$1 despite significant supply disruptions and the threat of a strike in Chile. Zinc prices have tumbled from over 80¢ a pound last summer to around 50¢. Soft prices spurred Doe Run Co., the biggest U.S. producer of lead, to cut back production recently and caused Reynolds Metals Co. to unveil plans to reduce aluminum output in Oregon. And steel prices, which rose last winter because of fears of a USX Corp. strike, which never materialized, continue to deteriorate.

The positive aspect of this picture, of course, is that it bodes well for inflation, if not for a buoyant recovery. Indeed, Robert H. Lesemann of Resource Strategies Inc., a metals consulting firm in Exton, Pa., believes the resilience of metals prices in the early stages of an upturn has been exaggerated, since dur-

SOME BIG WINNERS IN A WEAK HOUSING RECOVERY

Housing analyst Barbara K. Allen of Kidder, Peabody & Co. recently reduced her estimate of housing starts for 1991 from 1.22 million units to 1.05 million—mainly because the industry is facing severe capital constraints from lenders. Yet she continues to favor homebuilding stocks, many of which have already doubled since last November.

The reason: It is the small private homebuilders who normally account for 95% of single-family housing starts, and they are being squeezed out of the market. Meanwhile, the large, publicly traded homebuilders have strong credit lines. "Even if housing demand doesn't jump as strongly as it did in prior recoveries," she says, "it will still be extraordinarily strong in relation to supply, and the big builders will benefit."

A similar explanation lies behind the price surge in the only industrial raw material that is riding high: lumber. Although demand for lumber is closely related to housing starts—and the current rebound in starts is one of the weakest in decades—lumber prices have soared by 50% this spring. Sparking the increase have been government plans to restrict access to some 40% of U.S.-owned forests in the Pacific Northwest, to protect the habitat of the northern spotted owl. The loss of that supply, say industry observers, means higher lumber prices and sharply higher profits for some forest-products companies, even if the housing recovery remains below par.

RETAILERS' SHELVES WON'T STOP SAGGING SOON

With consumer spending picking up, retail inventory-to-sales ratios are starting to decline. But that doesn't mean retailers are about to go on a stock-building spree in the months—years—ahead, cautions economist Richard B. Berner of Salomon Brothers Inc. Throughout the expansion of the 1980s, he notes, retail inventories soared to unprecedented levels because of an explosion in retail outlets—in response to the surge in consumer spending after the 1982-83 recession, favorable tax laws and the ready availability of financing.

From 1982 to 1987, for example, traditional retail establishments (excluding mom-and-pop stores, which grew ever faster) multiplied at a 2.5% annual clip. That's five times faster than the growth rate in the previous 20 years. By contrast, the growth rate for real consumer goods purchases increased much more slowly, from a 2.8% annual pace to 4.6% or by only about two-thirds.

The upshot was vast overexpansion in both outlets and the inventories needed to stock them—and soaring inventory-to-sales ratios, despite the growing use of such devices as product scanners at checkout counters to keep inventories under control. And as Berner sees it, the shakeout in retailing that began a few years ago still has to run its course before ratios are pared back to healthy levels. "The process," he says, "may drag on for some time, dampening the pace of the recovery."

SMALLER SLICES OF THE PAYCHECK FOR 401(k) PLANS

Evidently, even tax-deferred savings plans have been affected by Americans' tendency to squirrel away less of their income. A survey of 1,518 U.S. companies by Massachusetts Mutual Life Insurance Co. reveals that so-called 401(k) plans, which allow employees to save part of their pay on a tax-deferred basis, are growing in popularity. But the percent of pay that workers are contributing to such plans has been falling. From 1988 to 1990, the average amount contributed by highly compensated employees fell by 6.8%, while the average contributions by workers at the lower end of the pay scale declined 6.1%.



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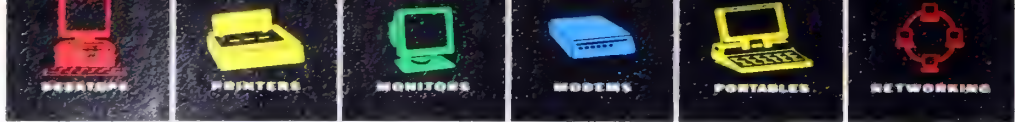
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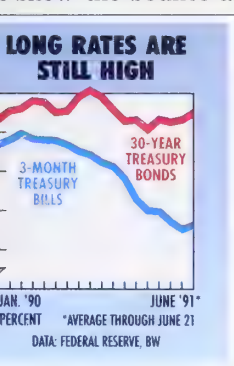
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HIGH RATES COULD KEEP THE RECOVERY IN ITS CRADLE

The U.S. economy is headed toward recovery with a lot of excess baggage. The recession did little to lighten the load of heavy debts, unsold real estate, shaky banks, and fiscal disarray in Washington and many states. That's weight enough on this fledgling turn, but the heaviest of all might be long-term interest rates. Although the Federal Reserve Board has cut short-term rates, long rates remain stubbornly high. Long-term interest rates influence the credit-sensitive demand for cars, homes, and other high-priced consumer goods. These are the kinds of cyclical items that lead recoveries and give the business cycle its swing. Clearly, the latest data on car sales, home buying, and durable goods orders are looking better, but the numbers still do not show the bounce associated with a normal recovery.



Long rates are under strong upward pressure. Any bond trader can tell you why. For the next few months, the U.S. Treasury will be in the bond market asking for about a billion dollars a day. States and municipalities will also have their hands out. And capital markets around the world are growing every day. On top of that, the private sector has to finance an economic recovery that traders fear will fuel inflation. Will people buy all this paper? Only if yields are high enough. Long-term rates will fall only if the recent signs of economic strength start to fizzle, or if the price indexes show stunning improvement in inflation. That means the chance that the economy may have to pay for lower rates on mortgages and other consumer and business loans may well be a lackluster recovery that will keep the credit markets unclogged and price pressures down.

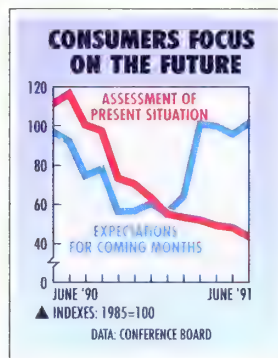
DEMAND SLOWS ON THE SLUGGISH SIDE

For now, the recovery is concentrated on the output side of the economy, as opposed to the demand side. That's because companies' vigilance over inventories has

kept them pretty downbeat about the here and now. However, this process will lead to a full and lasting recovery only so far as demand growth allows. That's where consumers hold the key, and high long-term interest rates are only one of the obstacles that will be blocking a consumer rebound in coming months.

So far, businesses are getting extra output from the same employees. Unless new hiring picks up, consumers' incomes aren't likely to rise any faster than their spirits. In June, consumers remained optimistic about the economy's prospects in the coming months, but job worries kept them pretty downbeat about the here and now.

The Conference Board's index of consumer confidence edged up to 78, from 76.4 in May. But the gain was concentrated in consumers' outlook for the next six months. The expectations index rose to 101.1 last month, from 95.5 in May. The reading on current conditions, however, fell for the 10th month in a row, to 43.3, from 47.8 (chart).



The big concern is jobs. The Conference Board reports that 37.5% of those surveyed think work is hard to get, a jump from the 23.7% expressing that concern last summer. And only 8.6% of consumers feel jobs are plentiful. That's much lower than May's reading, and it's a sharp decline from the 23.4% who felt that way a year ago.

The latest data on state unemployment claims appear to verify the notion that jobs are scarce. True, new filings for jobless benefits have been falling since they peaked in March. But that only suggests that companies are laying off fewer workers. The total number of people who are collecting benefits continues to rise.

In early June, 3.6 million were receiving benefits, up by 136,000 from the previous week and the highest level in eight years. The large number of continuing claims means the economy is still not generating many new jobs, so people are finding it difficult to get off the unemployment line.

FACTORIES ARE STARTING TO HUM

Businesses will have to see a sustained pickup in demand before they start hiring again. And interest rates may have to fall a bit more before order books fill up fast enough for manufacturers to build up the production momentum necessary for a lasting recovery.

The latest news from durable-goods factories certainly looks encouraging. New orders for durable goods rose

Business Outlook

3.8% in May, to \$120.5 billion, on top of a 3.6% gain in April (chart). Although the April and May advances were broad, they were only moderate. Moreover, May orders were still about 7% lower than they were last summer.

DETROIT IS FINDING CAUSE FOR OPTIMISM

Shipments of durable goods also rose in May, by 1%, to \$121 billion. Most of that increase came from the auto sector, reflecting the recent upturn in new-car sales. Domestically made new cars sold at an annual rate of 6.5 million in mid-June. Sales for the first 20 days of June are running at about 6.4 million, an improvement from the 6.1 million pace of May, and the exceptionally weak 5.5 million rate in April.

The increase in car buying is paring inventories and creating some optimism in Detroit. Auto output is slated to rise in the third quarter. Carmakers are expected to produce about 6 million cars, at an annual rate. That's up from about 5.3 million in the second quarter, with most of the increase coming in July. Taken by itself, that would add about one percentage point to the annual growth rate of third-quarter gross national product.

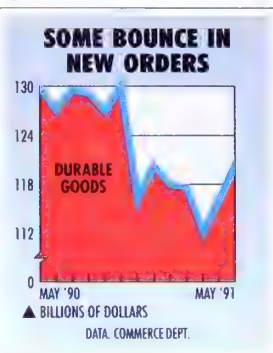
HOUSING CONTINUES TO GATHER STRENGTH

For other makers of durable goods, however, the summer may not be as busy. Even with the uptick in new demand, the backlog of total orders edged down by 0.1% in May and is 1.4% below its pace of a year ago. Unfilled orders for durable goods haven't risen since December, 1990. With the backlog of demand still falling, producers have little reason to boost output beyond what's necessary to fill current demand.

Manufacturers of capital equipment, in particular, could run into trouble if interest rates rise by much more. Orders for nondefense capital goods increased by 4.2% in May. But demand had collapsed earlier in the year. Excluding the booming aircraft sector, the backlog of unfilled orders is down 4.9% from a year ago. So while

capital-goods production may pick up in coming months, the rebound is shaping up to be pretty tepid.

Machine-tool makers, whose orders tend to foreshadow the path of capital-goods output, don't offer an encouragement. The Association of Manufacturing Technology reports that demand for machine tools, which are used by other manufacturers, fell in May for the fourth consecutive month. May orders totaled \$155.8 million, down 19.6% from April and 24.5% below their year-ago pace. Domestic demand is especially weak.



For the rest of the year, durable-goods manufacturing will be vulnerable to any upward shift in interest rates. The Conference Board's survey shows that consumers' buying plans for big-ticket items, such as appliances, are already weak. And higher borrowing costs would make businesses rethink their capital spending plans.

In addition, rising mortgage rates threaten to derail the housing rebound that is beginning to take hold. In May, sales of existing homes increased by 6%, to an annual rate of 3.5 million. That was the fourth solid gain in a row. Home prices are also rising a bit, another sign that demand is strengthening.

The danger is that higher rates could cause problems during the important summer selling season. A retrenchment would hurt not only homebuilders but the makers of home-related goods as well.

As the recent pickups in housing and autos show, high long-term interest rates aren't likely to prevent an economic recovery from getting off the ground. But on top of a shaky consumer sector, a glut of commercial real estate, weak banks, and deteriorating government finances, lofty long rates could easily keep the economy from flying very high.

THE WEEK AHEAD

NAPM SURVEY

Monday, July 1, 10 a.m.

The index of business activity compiled by the National Association of Purchasing Management probably rose to 46.9% in June, from 45.4% in May, according to a survey conducted by McGraw-Hill Inc.'s MMS International. The index has gained steadily since February, suggesting a recovery in the industrial sector.

CONSTRUCTION SPENDING

Monday, July 1, 10 a.m.

Spending on building projects was probably little changed in May, say the MMS economists. In April, construction spending rose 0.8%, but it had fallen a sharp 2.1% in March. Housing is on the up-

swing, but nonresidential construction continues to falter.

FACTORY INVENTORIES

Tuesday, July 2, 10 a.m.

Manufacturing inventories likely fell by 0.2% in May, the same decline as in April. Factory shipments rose by a stronger amount than production did in May. New factory orders likely rose by 3% in May, after rising 1.8% in April. Durable-goods makers have already reported a 3.8% rise in their orders.

NEW SINGLE-FAMILY HOME SALES

Wednesday, July 3, 10 a.m.

The MMS consensus is that new homes sold at an annual rate of 510,000 in May, a 2% increase from April's 500,000 pace.

The gain is suggested by the rise in existing home sales in May and the 3.1% advance in the starts of single-family houses.

EMPLOYMENT

Friday, July 5, 8:30 a.m.

On average, the MMS economists expect nonfarm payrolls to post a 31,000 increase in June. That would be the second modest rise in payrolls—a good sign of the recession's end. However, not all are convinced that the downturn is over—or that the recovery will be mild. The MMS survey results range from a 100,000 increase in jobs to a decline of 80,000. In May, nonfarm payrolls rose by 59,000. The June unemployment rate is projected to hold steady at 6.9%.

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JAPAN CLEANS HOUSE—AGAIN

THIS TIME, MARKET REGULATORS MEAN TO GET TOUGH ON SHADY PRACTICES

Saturday and Sunday are normally quiet days at Japan's hulking, gray stone Ministry of Finance. But not the weekend of June 22 and 23.

Rocked by leaked news reports that their firms had financed a major under-world figure and secretly covered \$464 million in losses by favored clients, top executives from Nomura Securities Co. and Nikko Securities Co. shuttled back and forth to the ministry to try to placate furious bureaucrats. But as Sunday dawned, it became clear that apologies weren't nearly enough.

The shocker came the next morning. Hastily calling a 9 a.m. board meeting,

Nomura President Yoshihisa Tabuchi, 59, said he was quitting as head of the world's largest securities house to "accept ultimate responsibility." Then Nikko President Takura Iwasaki, 62, followed suit across town. Says a Nikko director: "It was the price we had to pay to restore our credibility."

CRONYISM. With the 1988 Recruit Co. insider-trading affair that toppled the government of Prime Minister Noboru Takeshita barely put to rest, the latest scandal offers fresh evidence that the bureaucrats still have a long way to go to clean up the inbred Japanese markets. Involving widespread cronyism and un-

der-the-table favors, the scandal also demonstrates that many of the barriers discouraging U.S. and other foreign banks, brokers, and manufacturers from doing business in Japan still stand in the face of international pressure.

But if only for domestic reasons, the bureaucrats feel they must get tough. They are attempting to end the stock manipulation and real estate speculation that helped create a financial "bubble" in Japanese markets in the late 1980s. Finance Minister Ryutaro Hashimoto and Bank of Japan Governor Yasushi Mieno, two of the government's most powerful figures, are helping orches-

THE SCANDALS SHAKING JAPAN'S STOCK MARKET

39,000

37,000

35,000

33,000

31,000

29,000

27,000

25,000

23,000

21,000

NIKKEI STOCK AVERAGE



1988

JULY Prime Minister Noboru Takeshita and former Prime Minister Yasuhiro Nakasone linked to insider trading in Recruit Cosmos Co. shares



DECEMBER Recruit scandal spreads, Finance Minister Kiichi Miyazawa and Nippon Telegraph & Telephone Chairman Hisashi Shinto resign

1989

FEB.-MAR. Recruit President Hiromasa Ezoe and Shinto arrested for bribery

APRIL Takeshita resigns



MAY Vowing to stamp out land and stock speculation, Bank of Japan begins raising interest rates

JULY 1, '88

JAN. 6, '89

DATA: DRI/MCGRAW-HILL

te a surprisingly tough, rolling crack-
down against shady operators and a
huddle of established financial institu-
tions that fuel them with money. Nomu-
ra and Nikko were merely the latest in a
series of targets.

Japan's top regulators believe that
trying to wipe out 1980s-style specula-
tion excesses would undermine the very
heart of Japan Inc.: the \$3 trillion stock
market that has provided a constant
stream of cheap capital to a host of Jap-
anese giants for more than 40 years.
Ultimately, they worry that too much
speculation and funny-money games
could undermine Japan's competitive-
ness in manufacturing.

To accomplish their ends, the regula-
tors are prepared to inflict pain. Mieno's
constant attacks on stock and property
speculators, combined with his relentless
high-interest-rate stand, have helped
push the Nikkei average down 40% since
the beginning of 1990. With banks offer-
ing about 8% on risk-free certificates of
deposit, Japanese investors have little in-
centive to plunge into stocks. If the
crisis escalates, says Christopher M.
Chinison, a managing director at Salo-
mon Brothers International Ltd., the
Nikkei could even slip another 2,000
points during the coming months. "It

could be a long, hot summer," he says.

Even if the market holds fast, Japan's
bureaucrats are still willing to see some
of the nation's top banks and brokers
suffer a global plunge in credibility as a
result of their efforts. But whatever the
outcome, bureaucrats and financial
sources contend, the market and its big
players will end up on a firmer footing
over the long haul if the excesses are

The reforms are going over well with small investors, who have been badly hurt by the Nikkei's nosedive

finally kept under control. "They are
moving in the right direction," says Gil-
bert de Botton, a London-based money
manager and longtime Japan-watcher.
"This is going to reinforce confidence."

A LONG JOB. Restoring confidence is key
to the Finance Ministry's long-standing
public objective of gradually deregulat-
ing Japan's financial markets and open-
ing them to greater participation by
Western financial institutions (page 28).

While Japan's bureaucrats are eager to
make the financial markets more effi-
cient, they still want to remain firmly in
control. So the bureaucrats are likely to
proceed with a careful market liberaliza-
tion. Failure to do so could invite foreign
retaliation against Japanese banks, bro-
kers, and insurers, which have invested
billions in expansion overseas.

The housecleaning at home may drag
on for years, however. Analysts and
traders speculate that Japan's huge
trust banks and life insurers, which
manage hundreds of billions of dollars'
worth of stocks and bonds, may be the
next targets. These sources say the bu-
reaucrats want to determine whether
any of the institutions acted illegally to
boost returns for favored customers.

To be sure, some skeptics maintain
that the crackdown is little more than a
shadow play, another Japanese attempt
to impress outsiders without making
real changes. Both Tabuchi and Iwasaki,
for instance, will remain with their firms
as vice-chairmen and probably will con-
tinue to exert influence behind the
scenes. "This will be history in a couple
of months," smirks one Western banker
in Tokyo. And some critics contend that
meaningful reforms never will be imple-
mented as long as the hidebound *keir-*



RYUTARO
HASHIMOTO
Finance Minister, vows
tough with speculators



DECEMBER
Yasushi
Mieno
becomes Bank of Japan
Governor, pushes interest
rates even higher

1990

JULY Stock speculator
Mitsuhiro Kotani
arrested for rigging stocks

OCTOBER Sumitomo Bank
Chairman Ichiro
Isoda resigns amid illegal loans
to Kotani, others

NOVEMBER Sumitomo
Bank bails
out troubled Itoman Co., a
major land speculator



1991

APRIL Seeking evidence
of tax evasion,
police probe purchases of
millions of dollars worth of art



JUNE Four top secu-
rities companies
admit reimbursing clients for
losses. Nomura President
Yoshihisa Tabuchi resigns

DATA: FACTS ON FILE, BW

JAN. 5, '90

JAN. 4, '91

JUNE 25, '91

Top of the News

etsu system links big banks, brokers, and manufacturers in tightly knit corporate families.

Yet as the number of embarrassing disclosures mounts, more and more skeptics are coming to believe that bureaucrats are serious about wringing excesses out of the financial system, even if the reforms fall short of creating a full-fledged Western-style market.

The regulators' crackdown does appear to reflect a change in government and public attitudes. For decades, the Finance Ministry tolerated stock manipulation, greenmail, covert reimbursement

of trading losses, and other shady deals. It was one thing during the easy-money 1980s, when the big brokers were widely admired as the symbols of Japan's new wealth. But the blatant speculation of the late 1980s, with the Nikkei stock average soaring 500% and real estate prices exploding, proved too much even for the Japanese.

As high interest rates have pummeled the stock market, hard-hit small investors have started to rail against their brokers' favors to big clients. That has made it politically easier for Japan's top regulators to discipline errant banks and

brokers. "The commitment by the Finance Ministry to clean up the market is real," says Nikko Executive Vice-President Yasuo Kanzaki. "It will continue

So far, officials can claim some noteworthy successes. Their campaign traces its roots back to the Recruit affair, which the employment agency's former chairman, Hiromasa Ezoe, sought to curry favor with leading politicians by giving them inside information on a new issue of an affiliate's shares. Since then, the Finance Ministry has enacted an insider-trading law. And investigations over the past year have forced se

FOR FOREIGN COMPETITORS, THE SCANDAL IS SWEET

For many American investment bankers, the crackdown in Japan is welcome. For years, they struggled to break into the Japanese investment banking business. Several times, says one banker, he has been asked to give informal guarantees to potential Japanese clients that an American acquisition will be profitable for two years after the sale. When his bank wouldn't do it, Japanese investment banks would. "Business has been lost as a result of not complying with their requirements," he says.

Now, with the presidents of Nomura Securities Co. and Nikko Securities Co. resigning under government pressure after their firms made similar guarantees to big clients, the playing field for U.S. bankers and brokers in Tokyo is leveling. While Japan's crackdown won't wipe out all of Tokyo's shady practices, foreign firms believe Japan is slowly approaching Western modes of conduct. "It is good news," says Elizabeth Allan, who manages the \$360 million Japan Fund Inc. "The authorities are finally putting teeth in their regulatory role."

Even U.S. firms doing big business in Japan have long complained about such practices as Japanese brokers steering new stock and bond issues to favored local customers. In 1990, Salomon Brothers Inc. had a messy row with Nomura when the latter pressured key Japanese clients to drop underwriting deals with Salomon. Now, with Japanese competitors under fire, U.S. brokers such as Morgan Stanley & Co. are upbeat about making inroads, especially in fund management.

The scandal is a major setback for Japanese brokers in the U.S. The top houses are barely turning a profit on the \$1 billion they have invested in U.S. operations. Now, some must live with the tainted image that comes from dealing with gangsters. "It's very damaging," says a senior U.S. executive at a Japanese broker in New York. "It's like an American firm dealing with the Mafia."

The official worries that U.S. corporate clients, already alienated by market scandals in Japan, will take their

Japan's scandals. A Nomura official in New York says the SEC has made informal inquiries about whether the latest Tokyo improprieties have any U.S. connection. Another Japanese brokerage official says questions about corporate-disclosure standards of Japanese companies have prompted the SEC to delay a New York Stock Exchange plan to ease its requirements for foreign listings. The NYSE declined comment. The SEC's concerns may escalate after the publication of *Deceitful Practices*, a forthcoming book by former

Nomura executive John E. Fitzgibbon Jr. He charges that the broker's U.S. subsidiary failed to register some employees and skirted other U.S. regulations. Nomura declined comment.

SMALL VICTORIES. Japanese executives are leaning on Max C. Chapman Jr., Nomura Securities International Inc.'s co-chairman, to turn more profits, Nomura sources say. Tokyo opposes Chapman's big-bucks plan to make trading the cornerstone of its U.S. strategy. Nomura sources in New York say relations with



U.S. BROKERS WANT A LEVEL PLAYING FIELD IN TOKYO

financing business elsewhere. The 80 or so U.S. firms that have listed their stock in Tokyo through Japanese brokers since 1985 are frustrated anyway. Despite spending \$150,000 a year to maintain their listings, trading of their shares has been light. In the past five years, only about 10 U.S. companies, such as Levi-Strauss & Co. and Avon Products Inc., have sold shares of their Japanese subsidiaries in the Tokyo market.

The Securities & Exchange Commission also may be getting antsy about

merger maven Bruce Wasserstein are also strained. The firm bought 20% of Wasserstein Perella & Co. for \$100 million in 1988—but since then, the merger market has tumbled. Wasserstein declined comment.

As the Japanese flounder on Wall Street, Americans in Kabuto-cho, Japan's financial district, are bullish. Equal footing may take years, but even small victories are sweet.

By Leah Nathans Spiro in New York, with William Glasgall in New York and Karen Lowry Miller in Tokyo

top figures out of the executive

e.

Sumitomo Bank Chairman Ichiro Imai quit last October after admitting one of his branch managers had illegally diverted deposits to Mitsuhiro Imai, a politically influential speculator now on trial for stock manipulation. Imai's resignation, and that of Fuji Bank Chairman Taizo Hashida, was also due to the collapse of Itoman Co., a textile company that borrowed \$6.5 billion in a disastrous real estate acquisition spree. The bureaucrats have also gone after brokers other than Nomura and Dai-ichi Kangyo Bank. Yamichi Securities Co. was fined \$990 for hiding payments to clients from tax authorities. Daiwa Securities admitted paying clients \$90 million to compensate them for losses last year. Even though Hashimoto and Bank of Tokyo-Mitsubishi continue to excoriate regulators, experts say the bureaucrats are not out to crush the securities industry completely. Analysts estimate payments to cover clients' losses have cost brokers as much as \$9 billion since the stock market peaked. In imposing a halt to such practices, "the Finance Ministry did the brokers a favor," says Deutsche Bank's Tokyo-based economist, Kenneth S. Courtis.

They need one badly. Even without their payoff woes, the brokers are having a hard time. With the Nikkei languishing, Tokyo trading volume has slowed to a third of its precrash pace. The slowdown pushed the four biggest brokers' earnings down 70% in the fiscal year ended Mar. 31, the worst drop in 15 years. In the past year, the industry has slashed its payroll by 7%, or 11,840 employees. What's worse, as the market has fallen, the brokers' most lucrative corporate accounts have evaporated. In boom years, insurers and trust companies kept as much as \$250 billion in funds with stockbrokers. Confident the market would keep rising, the brokers improperly guaranteed custom-fat profits in advance in return for the right to invest the funds as they saw fit.

ASSURE. In Tokyo's roaring bull market, covering the occasional trading loss was usually a snap. But the game began to wind down in 1989. First, the Finance Ministry tried to limit profit guarantees through a loosely worded law—with little effect. Then, the ministry pressured brokers to discontinue the accounts altogether. By April, 1990, with the Nikkei already down 23% from its peak, brokers sold off all but \$29 billion worth of funds' assets. But this spring, with the market down another 15% and corporations preparing to close their books for the fiscal year, customers started pressing brokers to make good on their profit guarantees. Many did, figuring

SUDDENLY, THE JAPANESE MOB IS OUT OF THE SHADOWS

Japan's gangsters are easy to spot: They're missing fingertips from a ritual act-of-contrition amputations. Sometimes their neck-to-knee tattoos of intricate dragons and cherry blossoms can be glimpsed as well. On street corners in neon-lit districts of Tokyo, the *yakuza* can be identified by their short, stiff, permed hairstyles, semidark sunglasses, dark polyester suits, white shoes, and light ties. Their cars also are distinct. Tokyo bosses have switched to cream-colored Mercedes-Benz models, while groups in Osaka still drive even more obvious Lincolns and Imperials.

The National Police Agency estimates that Japan's underworld is home to some 3,300 *yakuza* gangs with nearly 90,000 members. They make more than \$10 billion a year from a combination of extortion, drug trafficking, debt collection, and prostitution. They also specialize in terrorizing land owners into selling out. Another specialty is getting the goods on a top executive and threatening a noisy confrontation at the annual shareholders' meeting if they aren't paid off.

WINKS AND NODS. Like U.S. mobsters, the *yakuza* have become more active in opening legitimate companies as fronts. That's one factor behind the forced resignations of the presidents of Nomura Securities Co. and Nikko Securities Co. Wink-and-nod deals to cover stock losses of favorite clients have long been tolerated. But buying \$29 million worth of memberships in a golf club owned by Susumu Ishii, retired godfather of crime family Inagawa-kai, cost the presidents their jobs. Nomura and Nikko were also blamed for lending Ishii huge sums, and Nomura was cited for helping him manipulate the shares of railroad company Tokyu Corp. Both deny wrongdoing.

One reason that dealings with the *yakuza* strike a nerve is that the gangsters helped fuel the steep rise in real estate and stock prices in the late 1980s, hurting smaller investors and

pushing the cost of homes out of reach for many Japanese. Cash was funneled through land, golf-club memberships, or stocks. Traders estimate that some \$3.6 billion of *yakuza* loot is still in the stock market—about half the 1989 peak. Traders say Kobe-based Yamaguchi-gumi, Japan's largest crime family, with more than 26,000 members, is the most aggressive stock player.

CLOSING RANKS. The *yakuza* are also expanding overseas. Prosecutors in Hawaii and California have special units to handle them. And this month, Securities & Exchange Commission documents revealed that George

Bush's brother, Prescott, acted as a consultant for Ishii-backed companies in buying small American companies. (Bush declined comment.) Gangs are also closing ranks in Southeast Asia to smuggle weapons, recruit prostitutes for Japan, and horn in on the Golden Triangle drug trade.

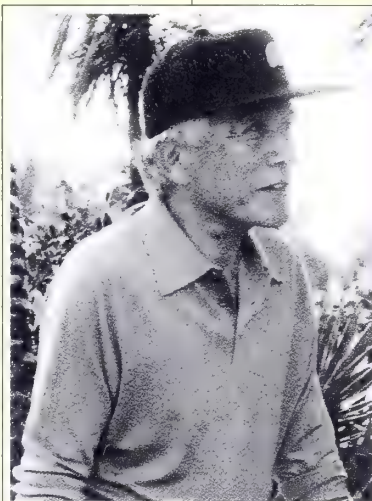
It's highly unlikely that Japan's law-enforcement officials will ever subject the *yakuza* to the same pressure the Mafia has faced in the U.S.

One reason is that the *yakuza* are a big source of funding for powerful right-wing, nationalist politicians. They're also radically pro-emperor.

Police are handcuffed in going after the *yakuza* because it's illegal for them to go undercover. Until recently, they weren't empowered to investigate a business just because a gangster owned it. In May, Japan's parliament passed an antimob law that gives cops and prosecutors more clout to prevent *yakuza* from infiltrating mainstream businesses. But no one expects a frontal assault anytime soon.

Some Japanese admire the *yakuza* for their feudal concepts of loyalty and duty. And the *yakuza* aren't very violent. Turf battles are on the rise in Tokyo as the Kobe mob tries to move in. But ever sensitive to public perception, crime bosses have been known to call press conferences to apologize for letting the skirmishing get out of hand.

By Karen Lowry Miller in Tokyo



CRIME BOSS ISHII RECEIVED HUGE LOANS FROM NOMURA AND NIKKO

that the bureaucrats would not object.

But the brokers classified the payments as trading losses or business expenses in a bid to reduce their taxes. That angered the ministry's taxation agency, which saw the move as an attempt to evade taxes. The agency started drumming up public support by leaking stories to the press that characterized the brokers as tax cheats. Then came an unattributed report in one of Japan's major dailies that Nikko and Nomura channeled funds to Susumu Ishii, the retired kingpin of a major *yakuza* crime group (page 29), by purchasing golf memberships worth \$29 million. That sparked the fire storm that forced the presidents of Nomura and Nikko from their jobs.

Despite the surprise resignations, even the limited change that Japan's bureaucrats have in mind will come slowly to Kabuto-cho, Tokyo's Wall Street. Nomura's new president, Hideo Sakamaki, has been Tabuchi's right-hand man for the past several years, serving as the broker's liaison with the Finance Ministry and playing a key role in realizing Tabuchi's dream of becoming a global investment banker. Like Sakamaki, Nikko's new president, Kichiro Takao, is a low-key veteran administrator with an appetite for international business.

DEAD SET. The crackdown won't immediately change the Tokyo market's unique style, either. Even in the face of increased regulatory pressure, brokers still appear to be manipulating—or "ramping"—stocks. On May 16, Nomura underwrote a \$100 million bond issue for Tokai Kogyo, a construction company. Attached to the bonds were warrants convertible into Tokai stock. Over the next month, although the Nikkei fell 3.8%, a wave of buying pushed Tokai Kogyo shares up 41%. That meant that anyone buying the bonds and warrants at the initial offer stood to reap an immense windfall. Nomura accounted for about a third of the Tokai purchases. But officials deny ramping the stock.

It will take time to root out such entrenched practices. But the Finance Ministry is dead set on its goal of winning more global credibility for Japan's markets. That will require putting a lid on payoffs, ramping, insider trading, and other offenses. "The real problem is that unfair conditions existed in the securities market," Hashimoto said shortly after the latest scandal broke. "Japan should tackle the problem for its own good." If Hashimoto is true to his word, the clean-up at Nomura and Nikko will hardly be the regulators' last hurrah.

By Ted Holden, with Karen Lowry Miller and Robert Neff, in Tokyo, William Glasgall in New York, and bureau reports

PENSION FUNDS

IT'S THE STATES' TURN TO PLAY 'RAID THE PENSION FUND'

But the deficit-shaving move is raising hackles nationwide

Elnora E. Hoyt could barely contain her anguish. Her voice quavering and hands waving, the frail-looking 77-year-old retired school secretary pleaded with the 13-person board of the giant California Public Employees' Retirement System. "I'm trying desperately to stay independent," she says, ticking off her monthly bill for groceries, mortgage payments, and health insurance. "I had 57¢ left over last year." Jim Coan, a former union leader and state engineer, put it more bluntly: "I paid taxes for 40 years to support California," he bellowed. "Now, my money is subject to raiders."

One by one, nearly two dozen retired California state workers came to a government auditorium in Sacramento to decry what they see as the pillaging of their life savings. Only this time, it is California Governor Pete Wilson, and not a junk-bond-wielding financier, who intends to do the looting. Faced with the need to close a \$14.3 billion state budget gap, Wilson is looking longingly at the \$1.6 billion surplus sitting in the CalPERS coffers (BW—July 1). And he is hardly alone.

With states everywhere grappling with ballooning deficits, governors and legislators are scrambling to tap employee pension funds or cut back on contributions to avoid more painful budget cuts or tax increases.

INSTANT SURPLUS. Wilson's blatant money grab is easily the most controversial. But in states as disparate as Texas, Alabama, and Maine, government bean-counters are poring over their pension funds' books to look for extra cash or to delay payments to their funds. New York went a step further, altering the

method of funding its \$50 billion in employee pension funds. Overnight, the state created a \$9 billion surplus by postponing contributions until much later. That will cut by \$600 million the amount the state must contribute to its workers' pensions over the next two years.

It could also leave the state vulnerable in the future. "When that paper surplus is run down, the state will owe billions to the fund," says a spokesman for New York's Civil Service Employees Assn.



The CSEA has filed suit to stop the change, charging that, by law, surpluses are to be used to benefit state workers, not close the state's budget gap.

State officials, though, say that they have little choice. Maine Governor John R. McKernan Jr., faced with a \$1.2 billion deficit, decided against added layoffs or slashing medicaid and health care programs. Instead, he wants to defer \$133 million that had been earmarked for state pension fund contributions over the next two years. In North Carolina, even a boost in the cigarette

x, the lowest in the U.S., won't close the state's \$1.2 billion deficit. That almost certainly means retirees won't get a cost-of-living increase this year—for the first time in 20 years. California officials predict that 22,105 state employees could be laid off if Wilson can't tap the pension funds.

Such a threat is an example of the politicization of pensions. Another way of playing politics is to attempt, as both Wilson and Republicans in the Texas legislature have done, to shift control away from independent pension boards. This amounts to a naked grab for power," asserts California Treasurer Kathryn Brown, who would lose her board seat under Wilson's plan. "It goes against everything fiduciary representatives seek to protect."

The politicians have a precedent: West Virginia has been dipping directly into its pension funds for loans to finance teacher pay hikes. Cities are doing it, too: Nearly insolvent under the weight of a \$129 million deficit, Philadelphia let its payroll from January to March borrow \$75 million from pensions for Pennsylvania teachers and city workers. "In a perfect world, you wouldn't want to do this," says city assistant budget director Margaret C. Van Belle, but she's better, she says, than missing paychecks or debt payments.

SAFE UNTIL TOMORROW. The Philadelphia funds were paid back with interest. But other pension plans won't be so accommodating. Unions in California will probably file suit if the state legislature approves Wilson's planned raid. Protests by Alabama state employees stalled a plan there to reduce its \$150 million budget shortfall by scaling back fund contributions. Not that the state has given up. "We think we're safe until tomorrow," says David G. Bronner, chief executive officer of Alabama's retirement system. Bronner, like his colleagues in other states, is watching California closely. A Wilson victory would embolden not just governors. Just 10 days after the California proposal went public, New York City Mayor David N. Dinkins floated a plan to save that cash-strapped city several hundred million dollars this year by stretching out pension payments.

Washington will soon enter the fray. Representative Edward R. Roybal (D-Calif.), chairman of the Select Committee on Aging, is investigating Wilson's plan, which he calls an attempt to "divert the retirement savings of workers and retirees and leave them with empty promises." Elnora Hoyt knows the feeling. And if some of the country's deficit-ragued states have their way, she could have a lot of company.

By Eric Schine in Sacramento, with Joseph Weber in Philadelphia, Chuck Hawkins in Atlanta, and bureau reports

WHAT'S \$40,000, WEIGHS 5,000 POUNDS, AND COMES IN ONE COLOR?

The Hummvee—a gulf war colossus that will hit the streets soon

On July 1, drivers along Los Angeles' Sunset Boulevard had better brace themselves. That's when Arnold Schwarzenegger plans to arrive at the premiere of his new movie, *Terminator 2: Judgment Day*, driving a High Mobility Multipurpose Wheeled Vehicle, better known to gulf war devotees as a Hummvee.

To the delight of weekend warriors everywhere, the versatile vehicle, used in the war to haul weapons and soldiers, isn't just for muscular thespians. Its manufacturer, AM General, is readying a

proceeding cautiously with plans to commercialize. It won't take civilian orders until this fall and has set a limit of 1,000 Hummvees for delivery in June, 1992. With the vehicle's appeal to drivers who do off-road work, such as ranchers and construction contractors, Armour says the company, with annual sales of \$510 million, could eventually sell as many as 5,000 nonmilitary Hummers a year.

That may be a tad optimistic, especially since postwar euphoria is already fading. Besides, based on price, if not amenities, the Hummer is a luxury vehicle, and U.S. luxury car sales are sinking fast. In 1990, sales of luxury sport-utility vehicles, such as the Jeep Grand Wagoneer, Range Rover, and Toyota Land Cruiser, plunged 24%, to 20,728, notes Wendy Beale Needham, an auto analyst at Smith Barney, Harris Upham & Co. The Grand Wagoneer is no longer in production, and Range Rover of North America Inc. expects its sales to fall 20% this year, to slightly more than 4,000.

The Hummer has some unique disadvantages as well. At 5,500 pounds, it weighs twice as much as comparable vehicles; at 85 inches, it's about a foot wider than the Ford Explorer pickup. Its bulk pulls down its fuel efficiency to a mere 13.5 miles per gallon of diesel fuel. And its acceleration is less than hair-raising: "To go from 0 to 60, you don't need a clock, you need a calendar," sniffs a Range Rover spokesman.

AM General sees little risk in its sortie onto the commercial battlefield, though. Its Mishawaka (Ind.) plant now is operating at less than one-third of capacity, and AM General as a whole is barely profitable. So even a little extra business can make a relatively large impact on the bottom line.

Nor is AM General abandoning its core market. The company is in the second year of a five-year contract to supply the U.S. Army with 33,000 Hummers. Military sales "will remain our No. 1 business," Armour says. But with plans to sell a few thousand Hummvees a year to civilians, AM General also may give road warriors something new to cheer about.

By Lois Therrien in Chicago



EVEN IN CIVILIAN LIFE, THE HUMMER WILL REMAIN NO-FRILLS

civilian version of the Hummer to go on sale next year.

AM General, a subsidiary of LTV Corp., seems to have a modest hit on its hands. In the first two days after setting up a toll-free hot line in mid-June, the company fielded some 900 calls, from as far away as Singapore, from potential buyers and dealers. AM General will sell three models, ranging from a two-door canvas-top version for \$40,500 to a four-door hardtop for \$44,000.

NO AIR? Don't expect glitz for that price. Unlike the \$43,000 Range Rover, which features walnut dashboards and all-leather interiors, Hummvees are no-frills. AM General has padded the seats and upgraded the heating system. But the South Bend (Ind.) company isn't sure about offering air conditioning. And you can have any color you want, as long as it's tan. Explains AM General President James A. Armour: "It's important to keep the vehicle very spartan, very rugged, very much like a military vehicle."

Since the Hummvee's lack of amenities may limit its appeal, AM General is

THE SUPREME COURT: 'LEAVE IT TO THE STATES'

Its conservative rulings are working against Corporate America

You need sharp eyes to find Casey, Wis., population 400, in a road atlas. But the U.S. Supreme Court has put the rural hamlet squarely on the legal map, right in the center of a raging debate over how much regulatory clout cities and states can wield over business.

Back in 1985, Casey town officials adopted an ordinance that required residents to obtain a permit before spraying their land with pesticides. The rule enraged at least one resident, who made a federal case out of it—with the encouragement of pesticide trade groups. On June 21, the high court unanimously refused to toss out the statute, ruling that federal regulations governing the use of pesticides weren't broad enough to preempt similar local laws.

The Casey decision fits a pattern of judicial restraint in business decisions—the hallmark of a court that has handed more sway over business to states and municipalities. "It's very much a 'leave it to the states' philosophy," says Stephen A. Bokor, counsel to the U.S. Chamber of Commerce.

DUE PROCESS. It's a trend with an ironic twist. Business once hailed the court's new direction. Now, business interests, facing activist state regulators, must stand in line with pro-choice activists, civil libertarians, and opponents of the death penalty to seek relief from Congress. "The business community used to oppose federal regulation," notes Mark I. Levy, a Chicago lawyer who frequently argues cases before the Supreme Court. "Now, they're moving to the point where, if there is to be regulation, they would rather it be uniform." "Uniform" means "Made in Washington." The court will again address federal-state conflicts in the term beginning in October, when it considers if federally mandated health warnings on cigarette packs immunize tobacco companies from state liability suits.

Increasingly, the justices' narrow readings of legislative language—and constitutional protections—are working to the corporate world's disadvantage. In perhaps its most important business ruling of the 1990 term, the court upheld a \$1 million punitive damages award against a California insurer that defrauded an Alabama woman of \$4,000. Some justices in earlier decisions had suggested that the way juries award huge punitive damages may violate a company's right to due process. But the 7-1 vote instead yielded to the standards states set on jury awards.



A TOUGH TERM FOR BUSINESS

Key Supreme Court decisions

PACIFIC MUTUAL LIFE INSURANCE VS. HASLIP The court upheld a \$1 million punitive-damage award to an Alabama woman who suffered \$4,000 in insurance-fraud losses

UNITED AUTO WORKERS VS. JOHNSON CONTROLS The justices ruled that employers may not bar women of child-bearing age from jobs in which they could be exposed to chemicals that might cause birth defects

INGERSOLL-RAND VS. McCLENDON The court ruled that federal law preempts state claims in wrongful-discharge suits

TOIBB VS. RADLOFF The court extended the Chapter 11 provisions of federal bankruptcy law to individuals

EEOC VS. ARABIAN AMERICAN OIL The court said the 1964 Civil Rights Act doesn't protect U.S. citizens working abroad

DATA-BW

In weighing whether Congress meant to exclude states from regulating certain areas of commerce, the justices rely not only on the law's specific language but also on the legislative record. In the Casey decision, for example, Justice Byron R. White noted that the key committees with jurisdiction over the pesticide bill in effect asked the court to decide how federal law affected state and local regulations. Similarly, in *Ingersoll-Rand vs. McCleendon*, the justices ruled that Congress clearly intended for federal law to preempt state law in cases concerning pension benefits.

The court's rejection of judicial activism also showed up in a May ruling that

made it easier for mutual-fund holders to sue fund managers. Normally, in such cases, shareholders must notify the board before filing suit on behalf of other shareholders. But there is a "futility exception" that says that a shareholder can sue without first consulting directors if the stockholder knows consultation would be futile. In the case, *Kamen vs. Kemper Financial Services*, a federal appeals court had crafted new law by doing away with the exception, on the grounds that it had spawned too much litigation. The high court reversed, saying that the lower court had overreached itself.

TILTING. Overall, the session ended June 27 wasn't one that gave business much to cheer about (table). In a high-profile case, the court ruled that sex-discrimination laws prohibit companies from barring fertile women from dangerous jobs. And the justices ruled 7-2 that the First Amendment does not prevent a state from imposing a tax on cable television.

The court is even tilting toward the states in cases it chooses not to hear, a category that is growing in importance as the justices deliberately shrink their work load. In February, they declined to hear an appeal from a defunct New York company whose executives were convicted of endangering workers' health. The company and the executives had argued that the federal Occupational Safety & Health Act foreclosed such prosecutions by states.

All of this leaves business with few alternatives but to trek up to Capitol Hill. But lawmakers have shown little interest in reforming liability laws or curbing the federal racketeering statute, two issues

where business has fared poorly when the high court has tackled them. "It will be a very difficult regulatory situation if we're going to try to market products nationally, yet deal with possibly 80,000 regulatory jurisdictions," says a spokesman for pesticide maker DowElanco, an Indianapolis-based joint venture between Dow Chemical Co. and Eli Lilly & Co..

Corporate America was an early fan of President Reagan's policy of naming judges inclined to stick to the letter of the law. But recent Supreme Court rulings recall the old saw: Be careful what you wish for. You just might get it.

By Tim Smart, with Dean Foust, in Washington

SOMETHING SPECIAL IN THE AIR: HITCHHIKING VIPs

Company jets can deliver lots of goodwill in Washington

It was a request that any company trying to make friends in Washington would gladly oblige. On June 12, Beneficial Corp. chartered a six-passenger Gulfstream jet to whisk White House Chief of Staff John H. Sununu from a New Jersey GOP fund-raiser. The state Republican Party agreed to reimburse Beneficial \$142 for ferrying a guest.

"Sure, we said 'yes'" when the GOP led, says Beneficial spokesman Robert Wade. Transporting such a VIP "was for us." The request came just a week before the House Banking Committee began drafting a financial-services reform bill. Beneficial, which backs

Bush Administration's version of the measure, brought its Washington lobbyist Gary Perkinson, to New Jersey for a fund-raiser and put him on the plane to fly back to Washington with Sununu. The Chief of Staff and the lobbyist talked about hockey and problems in U.S. education—anything, both Sununu and Beneficial insist, except the financial-services business. "We were just trying to be accommodating," says Wade. Perkinson wouldn't comment.

So far, all Beneficial has gotten for its efforts is bad publicity. Although there's no evidence the company did anything improper, it has been singled by the controversy over Sununu's "fly now, pay later" approach to travel. But the episode revealed a fact of Washington life: One of the best ways to earn the gratitude and goodwill of busy officials is to let them travel on the corporate plane. Indeed, the game is sufficiently attractive that companies are willing to risk unpleasant legal, tax, and public relations problems just to play.

Although there's much joking about Air Sununu in Capitol Hill, lawmakers such as Senator Bob Dole (R-Kan.) and Representative Richard A. Gephardt (D-Mo.) are among the most frequent corporate fliers (table). For short-noise jaunts, members of Congress often request corporate flights. Candidates and accompanying aides must pay in advance, generally at the commercial first-class rate. But

that's only a fraction of the cost of a private charter.

Regulations in effect since March allow executive branch officials, including cabinet members such as Commerce Secretary Robert Mosbacher, to fly corporate planes on official business. The trips must be publicly disclosed twice a year—the first disclosure is due in October—and acceptance of the flight can't create the "appearance of improper influence." Again, compensation is paid at a comparable commercial rate.

Critics aren't impressed. Says Georgetown University law professor Robert Pitofsky, a Federal Trade commissioner in the Carter Administration: "Once you develop a policy where corporations can be generous to people in the executive branch, you run a serious risk that regulators will feel grateful and act accordingly." Pitofsky never took such flights.

EXPRESS MALE. Congress is making noises about tightening the rules on corporate flights. But Federal Express Corp. probably isn't worried. The Memphis-based delivery company, which declined to be interviewed for this story, is among the most active providers of corporate aircraft to official Washington. In 1988, FedEx delivered House Ways & Means Committee Chairman Dan Ros-

tenkowski to the capital from a Miami Democratic fund-raiser. Rosty arrived just in time to finish work on a tax bill—one that included a \$3 million tax break for Federal Express that Rosten-

kowski made sure was in the final measure. "They're the best at this," says one top Democratic congressional aide. "They serve cocktails and talk about baseball, knowing that later, when they need to be heard, they'll have the access."

Another company that frequently provides jets to government officials is Houston-based Coastal Corp., an oil and gas giant. "We have airplanes moving across the country most of the time," says John C. White, Coastal's Washington lobbyist and former chairman

of the Democratic National Committee. "There's sort of a code. You don't talk about business. It would be improper. But no senator or congressman ever gets mad at you for providing flights."

Most corporations that provide such on-call services have made a complicated legal decision. "This isn't something you just do," warns Nel Sanders of the National Business Aircraft Assn. The group counsels its members against providing flights to government officials and candidates. One reason: conflicting interpretations of the law by the Federal Election Commission and the IRS. The FEC says a candidate must reimburse jet operators, or both the company and the campaign could be cited for violating FEC regulations. But the IRS may then slap the companies with federal taxes that apply only to carriers that transport

paying passengers.

In the long run, persistence, doing favors for powerful friends, and coming through with some well-timed PAC contributions are still the preferred—or at least the safest—way for companies to snuggle up to Washington bigwigs. But the town's veteran lobbyists know there's nothing like the surge of power one feels taking off in a private jet to bring a smile to the face of a harried politician.

By Douglas Harbrecht in Washington



FLAK MAGNET: SUNUNU IS THE MOST VISIBLE BUT NOT THE ONLY OFFENDER

SOME OF WASHINGTON'S OTHER FREQUENT FLIERS

BOB DOLE (R-Kan.) The Senate Minority Leader has been a passenger on jets belonging to agribusiness giants ConAgra and Archer Daniels Midland and energy conglomerate Coastal Corp.

DAN ROSTENKOWSKI (D-Ill.) The House Ways & Means Committee chairman flew to Washington in 1988 on a Federal Express jet in time to make sure that a tax break for Federal Express remained in legislation

ROBERT MOSBACHER During the past two years, the Commerce Secretary has taken more than 20 domestic and foreign trips that were paid for by companies and foreign governments

RICHARD GEPHARDT (D-Mo.) The House Majority Leader used campaign funds to reimburse Archer Daniels Midland, Tyson Foods, Federal Express, U.S. Tobacco, and others for use of their jets

DATA: BW

Commentary/by Judith H. Dobrzynski

CUTTING LOOSE FROM SHAREHOLDER ACTIVISTS

A quick glance at the 1991 proxy season might prompt you to think peace has broken out between corporate management and activist shareholders. Sure, there were a few headline-grabbing fights—notably the attempt by dissident Robert A. G. Monks to win a board seat at Sears, Roebuck & Co. But even while Monks was losing, the number of proxy contests for board seats was declining. So were victories by dissidents. And this year, many executives who faced pesky shareholder proposals decided instead to bargain. Of the 153 corporate governance proposals submitted by institutions, only 101 came to a vote, according to Georgeson & Co., the proxy solicitors. Companies such as Avon, Xerox, and W. R. Grace volunteered to change their ways.

No question, that's progress. Says James S. Martin, executive vice-president of the College Retirement Equities Fund, which each year sponsors 10 or so resolutions: "There's a growing comprehension on management's side that we have real needs and that what we want is accountability."

PARACHUTES. But 1991 was not, by any means, a leap forward for shareholder activism. In fact, a closer look at recent developments reveals certain trends that may weaken the activist movement.

Those negotiated agreements, for one thing, are not all they're cracked up to be. In most cases, the companies agreed merely to adopt confidential voting of proxies. Secret balloting will curb management's ability to watch the votes as they come in and ask shareholders to reconsider. But giving in on this issue does little to improve management accountability. Worse, in many cases shareholders agreed to withdraw resolutions on other issues, such as blocking lucrative golden parachutes for managers, to win confidential voting. In the few cases—such as Avon Products Inc.—where management negoti-

ated the creation of a shareholder advisory committee, it's unclear just what the panel will do.

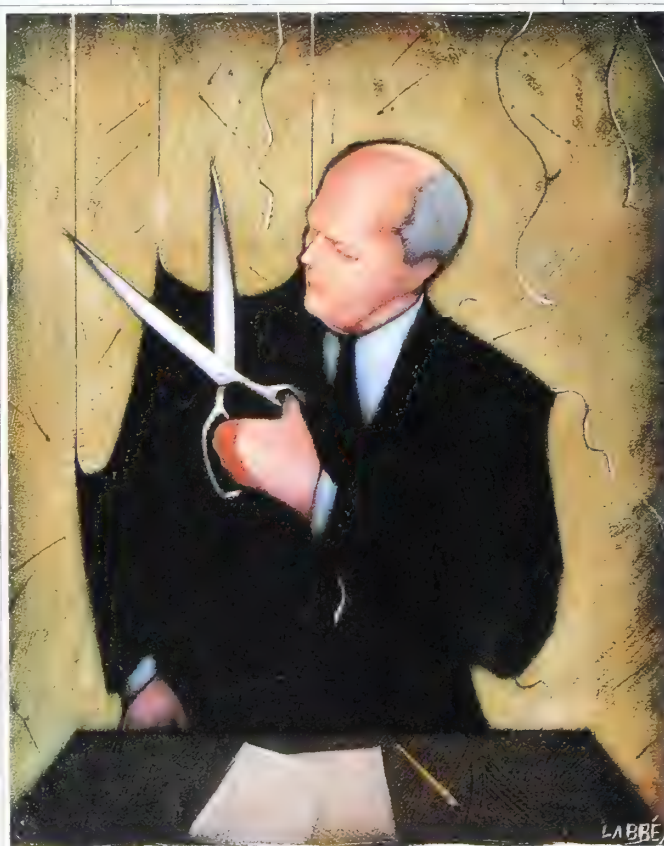
Troubles at the \$63 billion California Public Employees' Retirement System are also cause for concern. Public pension funds are the most vocal shareholder activists, and CalPERS Chief Executive Dale M. Hanson is the leader of the movement. As part of a state budget fight, Hanson is under pressure from Republican Governor Pete

says Gregg A. Jarrell, a former chief economist of the Securities & Exchange Commission now at the University of Rochester's business school.

Jarrell sees an even more damaging constraint on activism elsewhere: Because Delaware courts and many state legislatures have virtually removed the threat of hostile tender offers, the stick hanging over management no longer works. Mighty American Telephone & Telegraph Co., for example, needed five months to win NCR Corp., and whether NCR shareholders came out ahead for the wait is debatable. "Without an effective avenue for takeover entrepreneurs, the institutions can't be effective," Jarrell argues. "Without the ability to go over management's head with a tender offer, the system doesn't work."

'FREE RIDER.' The system does allow proxy contests to place directors on a board or to gain control of it. This year, dissidents won minority representation at Cleveland-Cliffs Inc. and Baltimore Bancorp. But proxy fights have problems of their own. They are riskier, more time-consuming, and more costly than tender offers. They offer no chance for an immediate payoff for the dissenter. Finally, they create the problem of the "free rider." A dissenter with, say, a 10% stake in the company foots the entire bill for the process but receives just 10% of any benefits.

To be effective, shareholder activism need not be confrontational. Next year will likely see investors continuing to focus on resolutions urging more independent directors and confidential voting. And they will try to make sure executive compensation is related to performance and monitored closely by outside directors. Such moves, however, can only go so far. Before activism regains its punch, shareholders may have to zero in on Delaware and the state legislatures—perhaps by pressuring corporations to give up their anti-takeover protection voluntarily.



Wilson to rein in his activities (BW—July 1). "What's happening in California shows that out-front activism among the public pension funds is limited by politicians," says Lilli A. Gordon of Gordon Group Inc., consultants. Hanson's difficulties will likely mute the activism of his peers, she says.

Wilson's attempts to gain control of CalPERS' board—throwing out representatives of the fund's beneficiaries in favor of political appointees—bodes ill, too. "If [a fund] can be sidetracked by politics, the whole reason for shareholder activism goes out the window,"

BRANIFF'S NEW
OWNERS HAVE
ALREADY INVESTED
\$10 MILLION



WHY STARTUPS CAN'T WAIT TO FLY THE RISKY SKIES

Cheap jets and willing investors are inspiring new carriers to wing it

But aside the wind-in-the-hair romance of it, and the recent history of startup airlines in this country is hardly inspiring. Witness the wreckage of such bold ventures as People Express Airlines Inc. and Presidential Airways Inc. Come to think of it, there isn't much to recommend anything with wings and engines these days. After 10 months of industry turmoil, even United and American are black and blue. But hope springs eternal in the airline industry. Perhaps the miracle of hurrying tons of metal through thin air is inspiration enough. Forget the bankrupt courts. Cast off those grim reminders of past aviation failures. With "niches" and cheap airplanes beckoning, suddenly there's a rush to launch new airlines.

WINGS OF DESIRE. Fledgling ventures are popping up everywhere. Braniff International Airlines Inc.—the namesake of the once-bankrupt, once-liquidated former carrier—will fly used narrowbodies out of Dallas and Long Island's Islip. Baltia has won Transportation Dept. approval to fly from New York to the Soviet Union. Groups of former airline executives are pushing plans for small carriers based in under-served Reno, Nev., and Kansas City, Mo. And 170 former Eastern pilots in Atlanta are spending \$5,000 each to try to launch a regional carrier to fill the void left by Eastern's demise.

The lure is a flood of inexpensive airplanes. Hundreds of

jets have been grounded over the past few quarters, driving down used-aircraft prices. Many planes are owned by lessors eager to see them fly again. "These people have airplanes coming out the garages," says Lee Hydeman, a long-time aviation attorney and board member of fledgling Reno Air. They're tempting startups with inexpensive leases.

Raising working capital is the hard part. Still, these fledglings are finding surprising allies. Baltia is run by Igor Dmitrowsky, a Latvian immigrant who used to run American Kefir Corp., a yo-

REVVING UP FOR TAKEOFF

BRANIFF	Dallas to Newark and Los Angeles; Islip, N.Y., to Orlando and Fort Lauderdale
BALTIA AIR	New York to Leningrad and Riga, with connections to Minsk, Kiev, and Tbilisi
RENO AIR	Reno, Nev., to various cities in California and along the East Coast
KC AIR	Kansas City to Dallas, St. Louis, and Minneapolis



gurt business. One of Baltia's top advisers is Harold J. Pareti, a former top executive at both People Express and Presidential. Dmitrowsky's lack of experience and Pareti's track record may stir questions. But exclusive routes to Leningrad and Riga have enticed investors. A Houston firm has placed \$148 million in debt to pay for planes. And the Delaware Insurance Commission, hoping to create jobs in the state, is helping to line up \$50 million in funding—though a deal is far from done.

RUBBER CHECKS. Reno Air, which hopes to lure gamblers and skiers from California and the East Coast, is trying to raise part of its capital from local casino hotels in a rooms-for-equity swap. KC Air is hoping local businesses will invest in its efforts to give Kansas City its own low-cost commuter airline. Both ventures have planes lined up but still need more money. Says Michael Rudd, a KC Air principal, "Everyone is well aware of the disasters. It's a perception problem."

Using your own money is easier. But in Braniff's case, it's hard to figure why real estate investors Jeffrey R. Chodorow and Arthur G. Cohen are willing to risk it. After leading the former Braniff Inc. into bankruptcy a year after buying it from Chicago's Pritzker family in 1988, Chodorow and Cohen are coming back for more. They bought a bankrupt charter carrier called Emerald Air Inc., purchased the rights to the Braniff name out of its bankruptcy proceedings, and then mapped a strategy to undercut American Airlines Inc. and Delta Air Lines Inc. with low-cost, nonunion service out of Dallas. All told, they have sunk \$10 million into the new airline.

Helping them with their new investment—until Transportation objected—was Scot Spencer, a key player in the former Braniff. Spencer, 26, had been involved in two other airline failures before leading Chodorow and Cohen into their first Braniff investment. He was slated to become the new Braniff's marketing vice-president, but then Transportation officials balked at his record of arrests for writing bad checks. Spencer couldn't be reached for comment.

Even with such distractions, Chodorow and Cohen say their new venture—already profitable from its charter business—is on solid ground. But Pareti, who has learned plenty in the startup game, says the only way to survive is to avoid competing with the big guys. "The airline industry is full of ego cancer," says Reno Air's Hydeman. "You can survive if you don't get it and go off and do dumb things." Given the myriad examples of failure, it's a wonder that lessor is so hard to learn.

By Michael Oneal in New York, with Gail DeGeorge in Miami

**IBM, HEWLETT-PACKARD,
SUN AND COMPAQ
SHOULD CLASH
IN THE MARKETPLACE.
NOT IN THE
WORK PLACE.**

N A S F R O M D I G I T A L

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EDITED BY HARRIS COLLINGWOOD

DELTA PICKS THROUGH THE RUBBLE AT PAN AM

► In an effort to build up its North Atlantic service, airline sources say, Delta has decided to bid for Pan Am's New York gateway, its Frankfurt hub, and various European routes. Delta also wants the Pan Am Shuttle, but will forgo the carrier's Latin American system. It has flatly ruled out the merger proposal that bankrupt Pan Am sought.

Inking a deal is a long way off, though. Pan Am chief Tom Plaskett is in no position to hold out for a merger. But he has vowed that Delta will have to take some Pan Am workers as part of any deal. Meanwhile, Delta may run into demands from the federal Pension Benefit Guaranty Corp. that it help with Pan Am's huge unfunded pension liability. And creditors have invited Chicago financier Jay Pritzker to bid. Delta will get first crack at writing Pan Am's final chapter. But the book is far from closed.

FRITO LAYOFFS ARE LOOKING LIKELY

► Wall Street has been buzzing with rumors that Frito-Lay may lay off as many as 6,000 employees. And Frito says it has hired consultant McKinsey to help streamline the snack-food giant. But the company says it hasn't set any figures for layoffs.

Tell that to 34 new MBAs who thought they would work for Frito in the fall. On June 24, the company told them their jobs may not exist in October and suggested they accept work elsewhere. "We wanted to be honest with them," says a spokeswoman.

PACKED TO SET UP SHOP IN SOUTH AFRICA

► With the White House expected to lift sanctions against South Africa in July,

U.S. businesses are scouting for potential deals. A team of executives from Digital Equipment recently visited Johannesburg to meet with political and business leaders, though company policy rules out doing business for now. The American Chamber of Commerce in Johannesburg also says that Apple Computer, H. J. Heinz, and other consumer-products companies have expressed interest in establishing operations.

Republican congressional staffers say President Bush will wait until after the African National Congress meeting on July 2 before he acts. The President is hoping that by then, Pretoria will have released all political prisoners. The ANC is expected to modify its opposition to foreign investment.

NCNB RE-POPS THE QUESTION TO C&S

► Hugh McColl may get the last laugh. Two years ago, NCNB's acquisitive chairman offered to acquire Atlanta-based Citizens & Southern but was rebuffed by C&S Chairman Bennett Brown. Instead, Brown engineered a merger with Virginia's Sovran Financial. But all has not gone well. The stock price of C&S/Sovran has been in a long slump, mostly because of concerns over bad loans.

That has given McColl the

ROOM AT THE TOP—FOR RENT

The guy says: "Meet me at my office." You arrive at a posh address and are greeted by a receptionist seated behind an imposing desk. Then the person you've come to see rushes in late. You go to his tasteful yet impersonal office. He sheepishly pulls out of his briefcase a family photo, some brochures, and a paperweight and arranges them on the empty desk.

What gives? You might be in one of the 80 offices of HQ Headquarters Cos., a chain that rents out office space by the hour or by the month. Clients pay from \$15 an hour for a modest San Francisco setup to \$15,000 a month for a lavish New York suite. HQ boasts a long list of big clients, including Apple Computer and Hershey Foods, that need a business pied-à-terre. But it also serves small fry who only have fancy nameplates. They're magnetized, by the way, so they pop right off when the office's next occupant sets up shop.

opening he needed. C&S/Sovran confirmed on June 26 that the board has authorized Brown to meet McColl to discuss a merger plan. If an agreement is reached, it would create the second-largest U.S. bank, with more than \$115 billion in assets.

A B-SCHOOL GETS BIG BUCKS FROM ELI BROAD

► Eli Broad, 58, already has a New York Stock Exchange company named after him. Now, with a \$20 million gift to Michigan State University on June 25, the chairman of Broad Inc. will soon have his



name inscribed over the arches of a major business school.

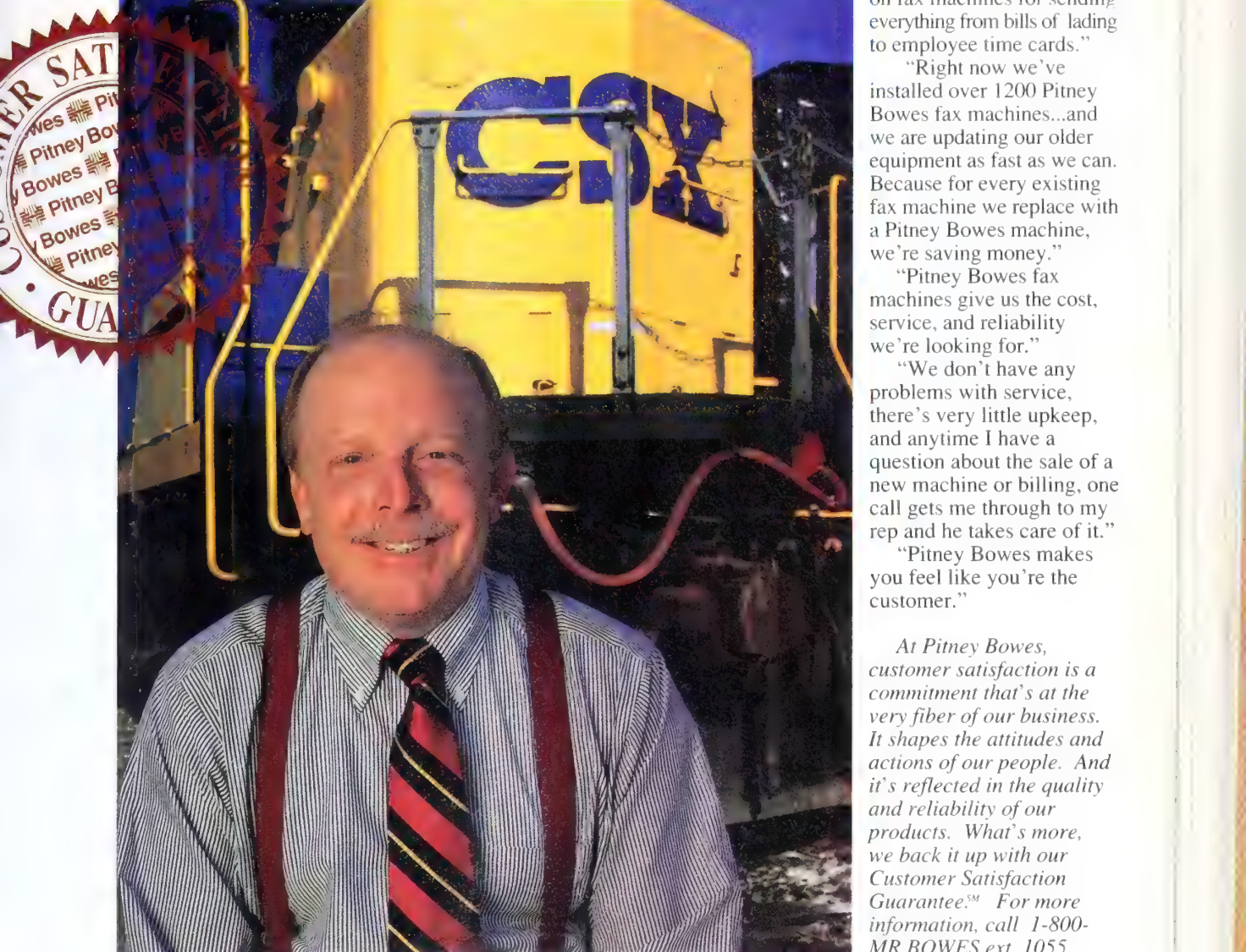
As a child growing up in Detroit, Broad recalls the aura of invincibility that surrounded General Motors. The region's decline so troubled him that he sought a way to "make a difference"—with the largest single donation ever to a public university's business school. "We need brighter people to go into manufacturing," says Broad.

PAT CHOATE TAKES TRW TO COURT

► Economist and author Pat Choate wrote a book last year about Japan's business lobbyists in America, called *Agents of Influence*. Choate's employer, TRW, fired him before the book was published but after complaints from prominent Japanese.

At the time of the firing, TRW Chairman Joseph Gorman told BUSINESS WEEK that Choate "sensationalized the subject matter." Now, Choate has filed suit against TRW, charging that the company welshed on a \$200,000 severance agreement after press accounts linked the firing to complaints by TRW's Japanese customers. TRW denies the charges.





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A GROUP ON THE MOVE.

Framatome consolidated net income rose sharply in the year ending December 31, 1990. Net income for the year increased to FF 984 million, a gain of almost 33 percent over the FF 741 million recorded in 1989 confirming the excellent profitability of our businesses.

Sales in 1990 reached FF 13.57 billion and were FF 1.87 billion up compared to 11.7 billion in 1989, a 16 percent increase excluding the fast breeder reactor Superphenix sale in 1989.

In the light of the Gulf War, which provided further proof of the instability of oil and gas resources, the nuclear industry looks more reliable and independent than ever before.

Nuclear power plants in the Western world operated excellently in 1990, thus continuing to prove their reliability. Nuclear service activity also increased in France as well as in the United States.

In France, the Civaux 1 order, for a 1450 MWe unit, shows the consistency of our country's nuclear commitment. The order for 18 replacement steam generators obtained by Framatome strengthened the company's chances of participating in future steam generator changeout operations, similar to the one conducted in France at Dampierre in 1990. This operation was an outstanding achievement in terms of completion time and radiation protection.

Framatome is monitoring the situation closely in Eastern Europe and the USSR. We are ready to assist in the improvement of existing nuclear power units, whenever possible, and in building modern units in full cooperation with local manufacturers.

In Asia, where we have a strong presence, the outlook for the nuclear industry is quite favorable. In the People's Republic of China, Framatome is actively pursuing the construction of two units in Daya Bay.

Framatome's partnership with Siemens through Nuclear Power International, NPI, is one of the keys of the nuclear business growth. Although the efforts made by NPI to export worldwide have yet to result in new orders, there is a growing confidence for the future.

Our non-nuclear activities contributed 37% of the consolidated revenue in 1990. In the later part of 1990, economic recession in the US and Europe hit the automobile, the electrical and the information technology markets. The 15% fall in the value of the USD also severely impacted the sales of Framatome Connectors International (FCI) as recorded in FF.

Our results in 1990 were not adversely affected by this slump thanks to a strong nuclear activity.

Finally 1990 was generally favorable to Framatome. Development of our activities, through a wider scope of businesses and increasing international scope is beginning to pay off. Our diversification has reduced the uncertainty of operating in a single industry while Framatome continues to expand its businesses worldwide.

Jean-Claude Leny
Chairman and Chief Executive Officer

CONSOLIDATED KEY FIGURES

- NET SALES	1990	1989
Net total consolidated (in FF million)	13,571	11,700*
Breakdown by industry segment: - NUCLEAR	63%	58%
- CONNECTORS	25%	31%
- MECHANICAL ENGINEERING AND OTHERS	12%	11%
Excluding the Superphénix fast breeder reactor sale		
CONSOLIDATED NET INCOME AND DIVIDEND	1990	1989
Group share of net income (in FF million)	984	741
Percentage of sales	7.2%	3.7%
No. of shares outstanding	10,000,000	10,000,000
Net income per share (French francs)	98.4	74.1
Dividend per share (French francs)	44.00	29.00

OUTSTANDING EVENTS IN 1990-91

- February 90 • Commissioning of CEMO (Equipment and Tool Maintenance Center).
- March-May 90 • Replacement of steam generators at Dampierre.
- May 90 • Purchase of Packinox.
- June 90 • Opening of the Framatome Connectors International (FCI) facility in Taiwan.
- July 90 • Delivery of reactor vessel and steam generators for Guangdong 2.
- August-Sept. 90 • Commissioning of Penly 1 and Golfech 1.
- October 90 • New shareholding: - CEA Industrie: 36.18% - EDF: 9.80% - Alcatel-Alsthom: 44.12%;
- Crédit Lyonnais Group: 5.00%; - Framatome personnel: 4.90%.
- November 90 • Licensing agreement with Mitsubishi.
- December 90 • Delivery of reactor vessel and steam generators for Golfech 2.
- January 91 • Booking of a complete Telescope for Korea.
- February 91 • Delivery of the Sizewell B 1 reactor vessel.
- March 91 • Delivery by Clextral of 2 twin-screw extruder for the new "paper pulp" line of Banque de France.
- April 91 • Booking of 18 replacement steam generators.
- May 91 • Delivery of 2,060 fuel assemblies by Framatome during the year 1990.
- June 91 • Nuclear services agreement with NFI in Japan.
- July 91 • Merger of Souriau and Burndy subsidiaries in the U.S. and France.
- August 91 • Sale of Técalemit by FCI.
- September 91 • Tunneller orders for Milan and Lyon.



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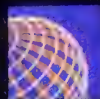
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BILL CLINTON: CAN HE MAKE IT OUT OF ARKANSAS?

It happens every four years. Democratic pollsters, fund-raisers, and think-tankers decide that the party's only hope for capturing the White House is to put a Southern moderate at the head of the ticket. With the Dixie Flash, they argue, the flight of Southern white males to the GOP will cease, and Democrats will be back in the Presidential ball game.

The difficulty in making this strategy work is that the Democratic nominating process is dominated by liberal activists and labor. So even though a big romp of early Dixie primaries seems to favor the emergence of a Southerner, the race is usually won in the big Northern industrial states.

But that hasn't stopped the Southern strategists' search for a champion. The old isn't promising. Virginia Governor Douglas Wilder and Senator Charles Robb have knocked each other out in a ugly squabble over bugged telephone calls. And Senator Albert Gore Jr. of Tennessee, who was the Southern hope in 1988, seems to be hanging back.

DIA MAGNETISM. That leaves Arkansas Governor Bill Clinton as the only Democrat who appears interested in running. He is getting a hard look from the would-be power brokers. Clinton's youth—he's 44—and his political base in underpopulated Arkansas make him an unlikely contender. But his activist governorship, and some strong performances on the rubber-chicken circuit, have created a bit of a Clinton ground swell. "He's the best promising young politician in America today," gushes Democratic activist Bill Galston.

A couple of years ago, few would have taken Clinton seriously. An interminable nominating speech on behalf of Michael Dukakis made him the object of national ridicule in 1988. Since then, Clinton has greatly improved his act. "He has really worked on it," says Democratic consultant Frank Greer,

who has advised the Arkansas governor. "We have only two politicians who are compelling on television. [New York Governor] Mario Cuomo is one. Clinton is the other."

What sets Clinton apart is his record of problem-solving. In three terms, he has turned the state's abysmal education and welfare systems into national models. He favors giving parents more choice in their children's education, tougher enforcement of child-support laws, and mandatory job training for welfare recipients. "Baby boomers," he says, "insist on more responsibility from those getting government help."

PLUCK. Clinton has a national platform as chairman of the right-of-center Democratic Leadership Council. At DLC gatherings, he preaches that government should forget social engineering and help people to succeed on their own. To appeal to the middle class, he backs a cut in Social Security taxes and higher personal exemptions for children.

Clinton's biography is a model of pluck: Born in Hope, Ark. A dirt-poor kid, he's raised by his grandparents. Young Bill works his way through Georgetown University, earns a Rhodes scholarship, graduates from Yale University law school. Then, he returns home and is elected governor at 33. Small wonder he's exciting the party's more conservative leaders. Maryland developer Nathan Landow says his fellow fund-raisers are excited about Clinton. "There's a lot of buzzing about him," he says.

But to convert the buzz into a serious Presidential candidacy, Clinton will have to find a way around the primary sink-hole that has swallowed up most Southerners in the past. For this problem, the Arkansas governor—who warns that the Democrats "can't continue as a national party" without an infusion of centrist ideas—hasn't found an answer.

By Douglas Harbrecht, with Susan B. Garland



CLINTON: A RECORD OF PROBLEM-SOLVING

CAPITAL WRAPUP

CIVIL RIGHTS

Efforts to avert a bloody Senate confrontation over job-discrimination legislation appear to be coming unglued. A group of moderate Republicans led by John C. Danforth (R-Mo.) has been negotiating with civil rights advocates and the White House in a search for a compromise. So far, Danforth has offered seven versions of the legal test plaintiffs must meet to win a discrimination suit. Six versions were acceptable to civil rights groups, but the White House balked. The White House can live with the seventh, but civil rights forces reject it. Meanwhile, Attorney General Dick Thornburgh, in

a six-page analysis of Danforth's efforts, says the proposal has "serious shortcomings."

REGULATION

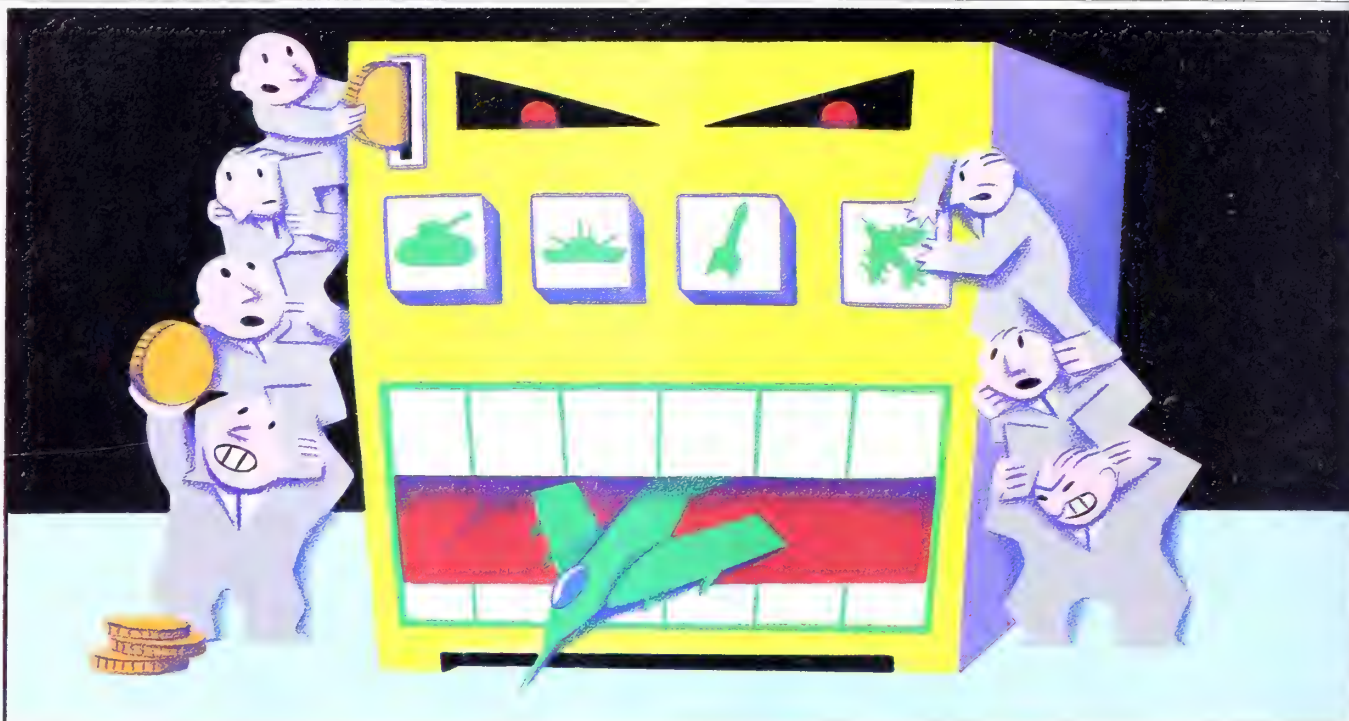
Food & Drug Administration Commissioner David A. Kessler's activist approach to drug regulation is running into flak within the Administration. The White House thinks he's going too far in his crackdown on companies that promote the use of prescription drugs for unapproved purposes. "It's incredibly paternalistic," grouches one aide. "It assumes that doctors don't know what they are doing." But so far, Kessler has not been ordered to back off.

BANKS

Bailout-shy lawmakers are continuing their search for the quietest possible way to keep the thrift cleanup and the bank deposit-insurance fund afloat through next year. The Bank Insurance Fund and the Resolution Trust Corp. need combined financing of up to \$200 billion through 1992. The scenario for minimizing publicity goes like this: Money for the nearly broke BIF is included in a House banking-reform bill. When the measure gets to the Senate, the thrift funding will be tacked on. The whole issue can then be resolved in a conference committee, avoiding a messy House floor fight.

EUROPE'S WEAPONS MAKERS LAUNCH OPERATION MARKET SHIELD

Cross-border deals now taking shape could lead to one-stop shopping for tanks, missiles, planes . . .



Mirage jets roar overhead, rattling the windows of the chalet overlooking Le Bourget airport and drowning out most conversation. But that doesn't stop silver-haired Sir Ralph Robins, chief executive officer of enginemaker Rolls-Royce PLC, from driving home his message. Sitting in the chalet rented for the Paris Air Show, he worries: "Violent changes are taking place in the defense industry."

Indeed, it's a nasty new world for Europe's weapons producers. First, it was the winding down of the cold war, which could prompt NATO countries in Europe to slash defense budgets by as much as 30% to 50% within five years. Now, the gulf war has sparked calls for tough controls on exports to once-promising markets in the Middle East and the Third World. Sales prospects in Western Europe's \$150 billion-a-year weapons business are so grim that a third of its 5 million workers could be laid off by the mid-1990s.

In response, the industry is already consolidating around a handful of Euro-

pean giants such as General Electric of Britain (GEC), Deutsche Aerospace (DASA) in Germany, and Thomson-CSF in France. Because of exploding costs and shrinking markets, they are under pressure to collaborate on defense programs to serve all Europeans. That's a big change. Formerly, every missile or tank was duplicated in some other nation's arsenal. After existing programs run out, says GEC-Marconi Co. Chairman Sir Geoffrey Pattie, who doubles as a Conservative member of Parliament, "I don't think we'll ever see single-country programs again."

SURVIVAL SKILLS. As a backup, a number of players are shifting from guns to butter. GEC and British Aerospace, France's Thomson-CSF and Aerospatiale, and Germany's DASA are stepping up diversification into civilian markets. In addition to cruise missiles and smart bombs, they're planning to make everything from smart credit cards that use microchips to video-phones and other telecommunications gear. Thomson is trying to offset its fast-declining sales of military electron-

ics components in the Middle East by expanding civilian operations in Europe and elsewhere.

But the key to survival is to become part of one of the new groupings. Rolls-Royce's Robins, who heads Europe's largest enginemaker, is proposing a wide range of military projects with France's SNECMA and Turbomecca, Fiat-Avio of Italy, and Spain's Industria de Turbo Propulsores. "I've always felt there should be a European engine industry," says Robins. Britain's GEC-Marconi is now deepening its missile-making involvement with France's Matra. Another possible missile combine would include DASA, Aerospatiale, and Matra.

GEC and British Aerospace, after linking up several months ago, now are bidding against IBM and British helicopter maker Westland PLC for the management contract of a proposed \$5 billion British helicopter program. British Aerospace and Germany's Messerschmitt-Bölkow-Blohm are working with Raytheon Co. of the U.S. to upgrade the Patriot missile. In Europe, the Eurosam consor-

of Aerospatiale, Thomson-CSF, Italy's Alenia, and newcomer Inisel of Spain is readying a similar antimissile program for the late 1990s.

The most ambitious of all cooperative efforts is the four-nation European Fighter Aircraft, which optimists say could generate total sales of 1,400 throughout the world. The critical issue of support from the German government is unresolved, but backing from the military and DASA should tip the balance in the U.S.'s favor. The new aircraft, however, would be a blow for France's Dassault, a British and military jetmaker. It has agreed to ring up a sale of its Mirage jet to the U.S. for three years, and its next fighter, the Rafale, won't be out until 1997, when the new European fighter will make its debut.

NATO's plans for a new rapid-deployment force in Europe are likely to spell more big changes. The force will place a premium on high-tech, high-powered weaponry and mobility. Europe's spending on research and development for defense already is growing at a double-digit clip, pointing to strong growth prospects in high-tech equipment, such as early-warning devices and stealth weaponry. What's more, the new NATO force may push defense manufacturers and their governments to begin standardizing equipment—a key way to save money.

WASHINGTON WOES. All this is stirring nerves in the Bush Administration. Officials worry that tight arms markets and removal of internal trade barriers within the European Community in 1993 could keep in place policies that favor local weapons makers. That would make it tough for U.S. defense contractors to win a new European business. At best, says Joel L. Johnson, a Washington lobbyist for U.S. aerospace interests, "we'd be pleased to hold our own [in Europe]." Not that there won't be some cross-Atlantic deals. The gulf war showed the need for advanced military airlift capabilities. And discussions are under way between European and U.S. plane builders to come up with a new, jointly developed military cargo aircraft.

Reshaping Europe's defense business promises to be a long process, with many bumps along the way. Often, it may be cheaper for Europeans to buy existing U.S.-made weapons, rather than pour billions into new systems. And NATO's influence diminishes, the Europeans will have to develop a new political group to coordinate defense planning. But if Europe wants to stay in the defense business, the most important step of all will be to put aside nationalist feelings.

By Richard A. Melcher in London, with Nathan B. Levine in Paris and John Templeman in Bonn

LOOK, UP IN THE SKY—IT'S TAIWAN'S SHIPPING TYCOON

Chang Yung-fa built one empire from scratch—so he's trying for two



TAIPEI: EVA AIRWAYS PLANE TO BUY 12.8 BILLION U.S. DOLLARS

Against heavy odds, Taiwan's Chang Yung-fa took one second-hand ship and in two decades parlayed it into one of the world's largest cargo carriers, Evergreen Marine Corp. Now 63, billionaire Chang is at it again. This time, it's in another tough industry: the airline business.

If he does to the airlines what he did to world shipping, competitors may be in for trouble. Chang wants to pull off one of the most daring undertakings in Asian aviation: launching a major carrier from scratch. After two years of ground work, his EVA Airways is scheduled to begin service on July 1, with flights from Taipei to Bangkok and Seoul. What's more, Chang has orders and options for 28 widebodies from Boeing Co. and McDonnell Douglas Corp. worth \$3.6 billion. "Nobody out here has tried starting up on such an ambitious scale," says William Burke, general manager of consulting firm Avmark Asia Ltd.

BEIJING CONNECTION? It's a gutsy move—especially in a crowded industry. But he has solid backing from Japanese banks that have financed Evergreen's ship purchases. The biggest plus is Asia's exploding demand in air travel, which is likely to continue growing at a 7% yearly clip for the rest of the decade. Taiwan is at the heart of the action: With more of its wealthy trotting the

globe for business and pleasure, traffic is growing by 12% to 15% annually. Out of the 2.9 million overseas trips by Taiwanese last year, a third were to China via Hong Kong. The flow could turn to a flood if Beijing and Taipei allow direct flights to the mainland, which some analysts think could happen within five years.

The government also is rooting for EVA. State-controlled China Airlines has been unable to fly many overseas routes because of inadequate capital and Taipei's lack of formal relations with most foreign governments, which are wary of up-

setting Beijing by granting landing rights. As a result, Taiwan ceded two-thirds of its lucrative overseas traffic to carriers such as United Airlines Inc. and Cathay Pacific Airways Ltd.

As a private company, EVA will have an easier time securing foreign routes. In addition to servicing booming Southeast Asian capitals such as Jakarta and Kuala Lumpur, EVA has a green light to enter Australia and Austria in September. Future destinations will include the U.S., France, Britain, and Germany.

Not that EVA is assured of a smooth ride. Some routes already suffer from overcapacity and low fares. And regional heavyweights such as Cathay Pacific and Singapore Airlines Ltd., the world's two most profitable carriers, are beefing up their fleets as well.

With Evergreen now boasting annual sales of more than \$1 billion, Chang has won respect despite his reputation as an eccentric tycoon. A vegetarian, he urges managers to join a religion known as the Duck Egg sect, whose adherents once relied on eggs for protein. He also believes in discipline: Being 15 minutes late counts as a day off—and most employees work well into the night. By running such a tight ship, Chang should also be able to make it in the skies.

By Pete Engardio, with Dirk Bennett in Taipei

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Nuclear energy means cleaner air.

FOR CHINA'S FREE-MARKETEERS, A STRING OF SMALL VICTORIES

Two years after the Tiananmen crisis, hardliners and liberals in Beijing continue to clash over control of the Communist Party apparatus and government policies. But while the heavies in Beijing do battle, China's army of technocrats and managers is engaged in a quieter struggle. Driven by China's vast need to raise capital and to overhaul clunky state companies, they are pushing ahead with piecemeal economic reforms. Their ad hoc measures fall short of the broad, free-market vision of Zhao Ziyang, the reformist Prime Minister and Communist Party chief who was deposed after Tiananmen. Still, "their cumulative effect is toward a more market-oriented economy," says Diane Yowell, research director at HongkongBank China Services Ltd. in Hong Kong.

In Shanghai, for example, Citibank, Bank of America, and four other foreign banks will soon open branches. Shanghai's business-minded leaders are bringing them in to get wider access to foreign capital and lure more companies to a foreign investment zone across the Huangpu River.

In Beijing, meanwhile, China VentureTech, a venture capital company with ties to the Finance Ministry and many financial institutions, recently joined with Britain's Standard Chartered Bank and stockbrokers James Capel & Co. to set up a new investment company. It aims to tap new sources of capital to buy shares in unlisted Chinese companies and eventually list them on stock markets in China or Hong Kong. And Chinese interest in Western-style management continues unabated. "Public rhetoric reflects the ideology after Tiananmen," says John M. Thomas, associate dean of the business school at New York State University in Buffalo, which sends professors to conduct seminars sponsored by U.S. companies in China. But among enterprise managers, he adds, "there's a tremendous interest in economic reform."

China's aging leaders show no sign that they will bend to threats by the U.S. Congress to curb trade if Beijing doesn't ease its political repression. But they recognize that there's an urgent need to improve economic performance. Although the economy is expected to grow 5% to 6% this year, China is still hobbled by huge subsidies, a crippling budget deficit, unproductive state industries, and a renewed inflation threat.

LAST GASP. Leader Deng Xiaoping is wary of political reform since Tiananmen, but he favors economic reforms—provided they don't risk social upheaval. So he continues to oppose

moves that could worsen unemployment or stir unrest, such as shutting down inefficient state industries. But for the first time in 25 years, Beijing recently raised grain prices for urban consumers—by 67%—to shrink farm subsidies. And housing subsidy cuts have boosted rents by as much as 60%.

Nevertheless, a political battle is heating up between Deng followers and last-gasp Marxist ideologues. Deng was believed to be behind the promotion of Zhu Rongji, Shanghai's liberal former mayor, to vice-premier early this year, and the recent appointments of three Zhao Ziyang associates as vice-ministers. But hard-liners struck back in recent weeks by sacking the head of a liberal economic institute and shutting down a reformist newsweekly.

The seemingly endless struggle will culminate in the 14th Party Congress in June, 1992—unless the political balance is tilted before then by the death of Deng, 86, or other Long March veterans. Promotions such as Zhu's are part of the old guard's efforts to position younger candidates for the succession. Until then, piecemeal reforms are at least steps in the right direction on the long road back from Tiananmen.

By Lynne Curry in Beijing and Dinah Lee in Hong Kong



SHANGHAI IS LURING MORE FOREIGN INVESTORS

GLOBAL WRAPUP

SOVIET UNION

Will the nearly worthless ruble become a convertible currency? That's what Prime Minister Valentin S. Pavlov is saying. Starting Jan. 1, the ruble will trade for hard currency within the Soviet Union, Pavlov promises, in an expanded system of auctions run by the Soviet State Bank. The aim is to make hard currency "easily available" to Soviet enterprises to pay for imports. At weekly auctions already being held by the State Bank on a small scale, the ruble last sold for 2.4¢.

Expanded ruble convertibility could boost foreign trade and spur competition for state monopolies by giving cus-

tomers the option to buy foreign goods. Paradoxically, Western-Soviet joint ventures that have been selling goods and services to foreigners and Soviet citizens for dollars are likely to be hurt. On Jan. 1, the government aims to ban such hard-currency transactions inside the Soviet Union. Warns State Bank Chairman Viktor V. Geraschenko: "Joint ventures should sell [their products] for rubles."

EUROPE

To keep Europe in the high-definition-TV race, the European Commission may kick in \$600 million in subsidies over five years. The payments would compensate broadcasters for

beaming programs using HDTV as well as traditional signals. On June 26, the EC decided that all new broadcasts must be HDTV. The aim is to assure a market for products of electronics giants Philips and Thomson.

The compromise settles a dispute that lined up the governments of France and Germany, which back the HDTV makers, against Britain and other countries. The latter support broadcasters of traditional signals such as Rupert Murdoch's British Sky Broadcasting Ltd. Consumers will pay heavily, too. All large new TV sets will have to include expensive HDTV decoders, whether or not customers want to receive the programs.

1941



■ President Roosevelt encourages minority employment by ordering defense contractors to cease discriminatory practices in hiring; first such Presidential effort

1953

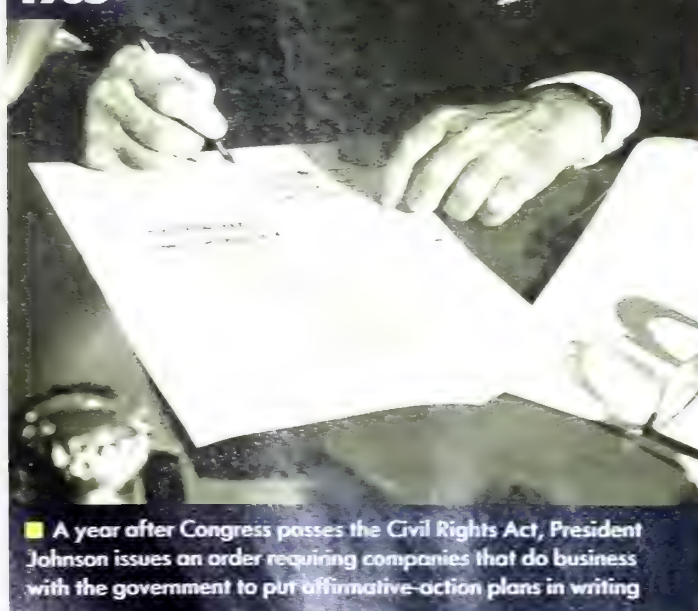


■ President Eisenhower creates a committee to receive complaints about discrimination, covering all federal contractors, including sub-contractors. Still no sanctions for noncompliance

RACE IN THE WORKPLACE

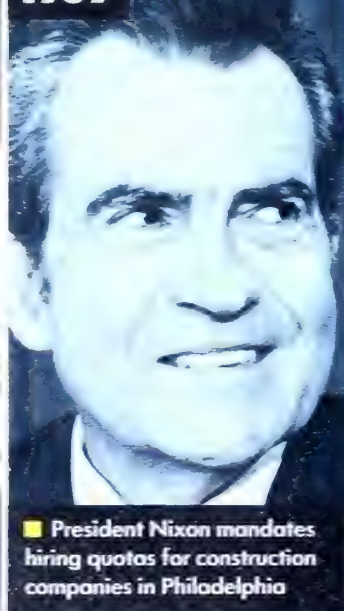
IS AFFIRMATIVE ACTION WORKING?

1965



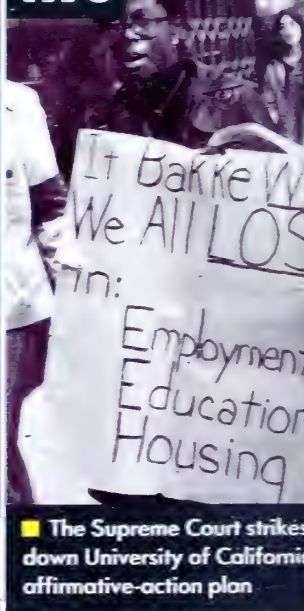
■ A year after Congress passes the Civil Rights Act, President Johnson issues an order requiring companies that do business with the government to put affirmative-action plans in writing

1969



■ President Nixon mandates hiring quotas for construction companies in Philadelphia

1978



■ The Supreme Court strikes down University of California affirmative-action plan



1963



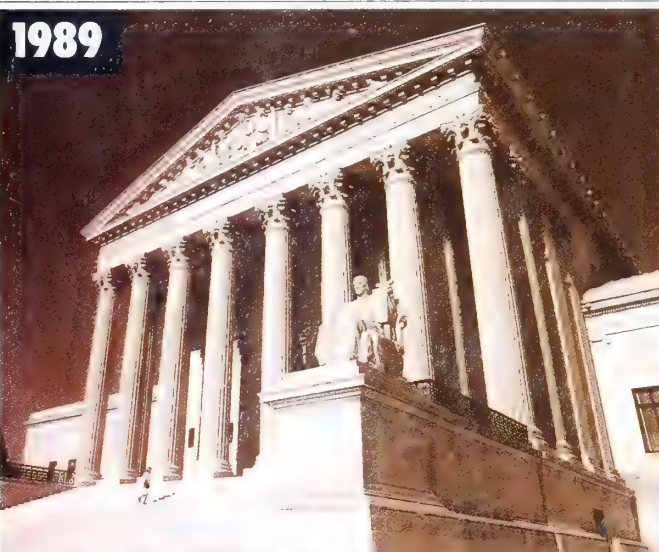
As the fight against segregation in the South intensifies, President Kennedy introduces the term "affirmative action" and puts teeth in minority hiring rules for government contractors. Creates commission to investigate contractors' practices, impose sanctions, collect employment statistics

■ Two hundred thousand blacks and whites rally in Washington for equal rights

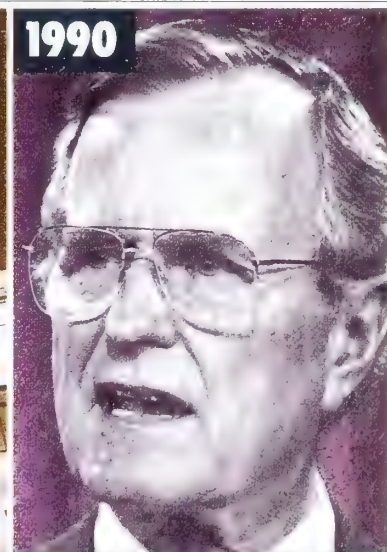
Every black person in every corporation has to ask: "If I were white, where would I be now?" —A black manager at Massachusetts Mutual Life Insurance Co. in Springfield
"Minorities get too fair a shake. And pretty soon we won't be able to afford the luxury." —A white stockbroker at Dean Witter Reynolds Inc. in New York

Call it affirmative action. Or minority outreach. Or perhaps you prefer "managing diversity,"

the newest, politically well-scrubbed name for policies aimed at bringing minorities into the business mainstream through preferential hiring and promotion. But however you describe such hiring based on race, U.S. society must come to grips with a sobering fact: Some 25 years into a national drive—and 50 years since the government first embraced the idea—to give blacks and other minorities a foothold in white, male-dominated Corporate America, the



1990



Justice General Meese
 es affirmative action in
 Court cases

■ The Supreme Court shocks civil rights groups with a string of decisions that make it difficult to win discrimination suits in court, triggering a national debate on hiring quotas

■ President Bush vetoes a civil rights bill that would have overturned five high court rulings

ideal of racial equality remains elusive, and the means of attaining it increasingly controversial.

Affirmative action encompasses both race and gender. Indeed, women have been among its greatest beneficiaries (page 62). But the discussion of race stirs the fiercest emotions. And as Washington's nasty partisan battle over the civil rights bills shows, affirmative action itself remains shrouded in ignorance, mistrust, and political cynicism. "The term conjures up the vilest of connotations," says Virginia Governor L. Douglas Wilder. "It has become like a four-letter word."

It wasn't always that way, of course. In 1964, the Civil Rights Act banned discrimination in employment and ordered that all hiring be color-blind. Affirmative action, established by a series of Presidential directives going back to Lyndon B. Johnson's in 1965, was to make up for past injustices, overcome continuing discrimination, and ultimately to provide equal job opportunities for blacks and whites. Unhappily, those aims sometimes contain a painful contradiction: Compensating for past discrimination against some people can create fresh discrimination against others. When companies make extraordinary efforts to hire or promote minority workers, they may penalize

OLD-BOY NETWORK. Small wonder that some companies have had trouble accepting the spirit of affirmative action. Not that business has entirely shirked its duty. Since the 1970s, most major companies and many smaller ones have adopted formal written policies to recruit minorities. Result: Affirmative action has produced major gains for black job-seekers. The percentage of blacks in the work force has risen by 50% in the past 25 years—a solid advance even taking into account a larger black population. The biggest gains were in the South and by black women. Many jobs came in government itself, where as many as 850,000 blacks found jobs in the social-welfare bureaucracy from 1960 to 1976. Huge numbers of blacks have moved into the middle class.

In 1989, about 5% of all managers in the U.S. were black. That's a fivefold increase since 1964 and a 30% increase since 1978. Still, there's a long road ahead. Nearly 97% of senior executives in the biggest U.S. companies are white. And while blacks make up 12.7%

of the private-sector work force, only 5% of all professionals are black.

Part of the problem for black managers is the so-called old-boy network. Jason Wright, a black vice-president at RJR Nabisco Inc., says: "The reality of life in America is that if you're white, most of the people you know are white. If someone says to you, 'Do you know anyone for this job?,' the people you recommend will probably be white."

Furthermore, overall progress seems to be slowing. After dramatic income gains in the 1960s and 1970s (chart), blacks have been losing economic ground for the past decade. And the good-paying manufacturing jobs that once were a doorway to economic security for working-class blacks are harder to come by in an increasingly service-based economy.

The idea that affirmative action isn't moving fast enough or far enough is reinforced by the widespread view in the black community that, ever since Ronald Reagan took office, Republicans have been using the White House bully pulpit to equate preferential hiring with racial quotas. Blacks feel, with some justification, that this is part of a deliberate political strategy to stampede blue-collar Democrats toward the GOP. "Prior to 1980, companies were learning to live with the new order," says John E. Jacob, president of the National Urban League. "After Reagan began to challenge affirmative action, companies began to question it." Result: a decade of backsliding and "a grade of C— for Corporate America," Jacob says.

While blacks fret that the drive for racial equality is slowing, many whites think it has gone far enough. In happier economic times, companies could give hiring preferences to blacks without

necessarily taking away white workers' jobs. That's much harder now. Corporate restructurings have slashed the ranks of middle managers, and new technologies have wiped out millions of low-skill jobs. Now, as the economic pie shrinks, whites increasingly begin to fear that affirmative action puts their careers in jeopardy.

DOUBTS AND QUESTIONS. Even those whites who still support affirmative action in principle think it can lead to too-rapid advancement of unprepared minorities. One white employee at United Technologies Corp.'s Hamilton Standard Div. in Windsor Locks, Conn., says he works for a black foreman who isn't up to the job—and is hurting his unit's morale. "I don't know if he's there because management thinks he's qualified, or because he's black," he says.

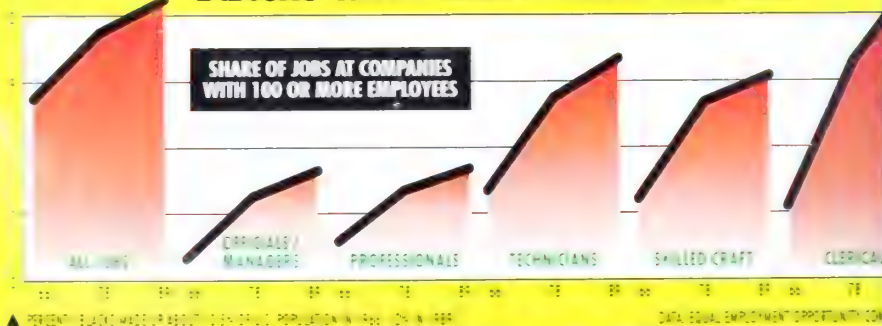
Whites aren't the only ones questioning race-based preferences these days. Some black intellectuals, such as Shelby Steele, who teaches at San Jose State University, say affirmative action works against their race. By singling blacks out for special treatment, Steele argues, it stigmatizes them as unworthy and creates a sense of victimization. Such feelings, he says, can stifle attempts to throw off the bonds of dependency and poverty that have plagued many blacks.

Other blacks are equally dissatisfied with preferential hiring, but for different reasons. They acknowledge that affirmative action has expanded opportunity but believe that many companies lose interest in black advancement once a hiring goal has been met. Some black middle managers feel they are being shunted into human resources or public relations—jobs that often spell "dead end" in the corporation.

It's not that way at every company, of course. Some corporations' commitment to equal opportunity goes far beyond lip service and a government mandate—not for altruistic reasons, but for pragmatic ones. Minorities, who now make up 28% of the U.S. population,

**MANY WHITES
ARE RESENTFUL—
AND BLACKS FEEL
AFFIRMATIVE
ACTION
HAS STALLED**

BLACKS HAVE MADE SOLID GAINS...



AVON CALLING—ON ITS TROOPS

At many companies, affirmative-action programs are top-down projects, sparked by the chief executive officer's interest. Some companies, however, respond better to a bottom-up approach. At the New York headquarters of Avon Products Inc., for example, all minority employees belong to in-house race-based networks—advocacy groups that have become a crucial part of minority relations at the company. "They constantly provide a barometer for us on how we're doing," says Yvonne Jackson, vice-president for human resources.

The Black Professionals Assn. (BPA), Avon Hispanic Network (AHN), and Avon Asian Network (AAN) developed independently of one another in the mid-1980s. At first, they were just social groups. But they soon evolved into self-help organizations devoted to encouraging minority recruiting and career development. Currently, Avon's 1,525-person work force is 13% black, 6% Hispanic, and 4% Asian.

The three networks, whose officers are elected annually by employee members, meet separately each quarter. Although they provide a source of support for staffers, they deliberately stay away from matters of discrimination or harassment. "We try not to use this as a complaint department," says Jose Agosto, president of AHN and manager of telemarketing services. Instead, they discuss such topics as lexictime and maternity leave.

GOOD RELATIONS. The network heads then take their agendas directly to CEO James E. Preston, President Rick Goings, and Ron Wolf. As chairman of Avon's Diversity Task Force, Wolf handles minority-related issues. One recent network victory: getting Avon to fund three-day seminars, outside the office, where minority employees discuss how to acclimate to Avon's predominantly white corporate culture.

"Sometimes, we challenge management—that's what we're here for," says Agosto. But usually, the Diversity Task Force is receptive to ideas, says Shirley Dong, presi-



AGOSTO, DONG, HALL: MINORITY NETWORKS PAVE THE WAY

dent of AAN and product counselor. It's this basic cooperation that allows Avon's networks to flourish, while similar groups at other companies have languished.

It isn't all business for Avon's networks. During Black History Month this year, the BPA hosted a trip to see the play *Mule Bone* by Zora Neale Hurston and Langston Hughes. Despite their advocacy role, says Sharon Hall, BPA president and director of new business development, the groups still like to get people together in a "nonconfrontational way."

By Heather Keets in New York

ve become a major force in the domestic economy, and businesses want to reach these growing markets.

"Corporate America isn't stupid," says Henry L. Warren, vice-president of planning and control at Arkansas Power & Light Co. "Companies are able to see that the customers they'll provide service to are changing." To serve these nonwhite customers, companies need a multiracial work force. Furthermore, for a company to ignore the ris-

ing numbers of minority workers—nonwhites now account for 22% of the labor market—is to let a valuable talent pool go untapped. Affirmative action "is not just the right thing to do," asserts American Telephone & Telegraph Chairman Robert E. Allen. "It's a business necessity."

But not all managers have come around to this enlightened view (poll, page 63). Many companies hire just enough minority workers to satisfy the

government and protect themselves against discrimination suits. "I've had people tell me, 'We need a woman for this,' or 'I need a black,'" during job interviews, says an investor-relations manager for a New York-based mining company. "Quotas will be set and met in certain staff jobs." (Many workers and executives interviewed for this story spoke on condition of anonymity.)

Black workers contend that once hired, they often meet with indifference or outright hostility. A black woman middle manager who has been with a large New York insurance company for 10 years complains that minority managers have a tough time advancing because plum jobs are often filled before they are ever posted. "It's Corporate America, and we didn't create it. It's their game and their rules."

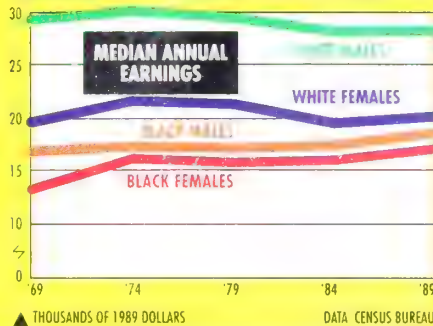
ASSEMBLY LINE. The current debate over proposed civil rights legislation produces only more anger and confusion. Democrats claim they merely want to restore the intent of civil rights laws by making it easier for minorities to win discrimination lawsuits. Republicans

BUT WHITES ARE STILL FARING MUCH BETTER

BY AS:	WHITES	BLACKS
MANAGERS	27.9%	16.5%
ADMINISTRATORS	31.6	7.4
TECHNICAL	12.3	23.1
WORKERS	25.6	30.3

INCLUDES PUBLIC- AND PRIVATE-SECTOR JOBS

DATA: BUREAU OF LABOR STATISTICS

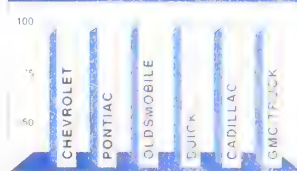


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Quality from the inside out.

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Our 3800 V-6 engine balances power, emission control and fuel economy with technological advances such as counter-rotating balanced shafts, electronic engine controls and sequential-port fuel injection.

Result: No U.S. carmaker builds better six-cylinder engines than the 3800 V-6 offered in many popular Pontiac, Oldsmobile and Buick models.

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ac is unsurpassed in customer action compared with any Euro- or domestic luxury nameplate.¹

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So it's not surprising that GM has the lowest average emissions of all American carmakers.²

In fact, it takes twenty-five 1991 models to produce the same amount of emissions as it took *one* model to produce 21 years ago. In terms of air quality, it's clear, GM has come of age.

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When you have to think about your car, something's wrong. With GM's automatic transmissions, there's little to think about. Millions of drivers have found them to be better quality and more trouble-free than all domestics and many imports, such as Honda and Mazda.¹ And GM's state-of-the-art electronically controlled transmissions



TRANSMISSION ENDURANCE TEST

have proven to be just as smooth after 100,000 miles of grueling taxi-fleet testing as when they were new.

These electronic wizards monitor a dozen different car and atmospheric conditions to perform quick, smooth shifts with maximum efficiency and utmost reliability—whether you're driving up snow-packed peaks or

through heat-baked deserts

A SURE START

The first sign of quality is a sure start. As thousands of tests have proved, our starting power is 99.9% sure every time you turn the key on your new GM car.

So it doesn't matter if you're in Maine or Mexico, in January or June, your new GM car or truck will start

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We are the only U.S. carmaker to design, test and manufacture brakes.

We design and test brakes to high standards for lining wear and fade-resistance.

As a result, owners of 1991 GM cars report fewer problems with their brakes than owners of Ford, Chrysler, Nissan, Mazda or Volvo.¹

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Today, there's a new commitment to quality in everything we do at GM. It's a genuine caring for you and a spirit of teamwork that pervades our



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- 1 1991 GM Customer Satisfaction Survey
- 2 Based on Mobile Exhaust Emissions Standards for passenger vehicles
- 3 Based on National Automotive Research Black Book for ten most recent available calendar years

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PUTTING QUALITY ON THE ROAD

Chevrolet Pontiac Oldsmobile
Buick Cadillac GMC Truck

are using the Democrats like a trampoline for pushing that most dreaded of all measures, a "quota bill."

In fact, the passage of the Democratic bill—or a GOP alternative—would make very little difference in how blacks are treated by corporations. That's because affirmative action is now so deeply ingrained in American corporate culture that changes at the margin of the law won't have much impact. The machinery hums along, nearly automatically, at the largest U.S. corporations. They have turned affirmative action into a smoothly running assembly line, with phalanxes of lawyers and affirmative-action managers. "Whether we have new civil rights legislation or not is irrelevant to us," insists AT&T's Allen, who earlier this

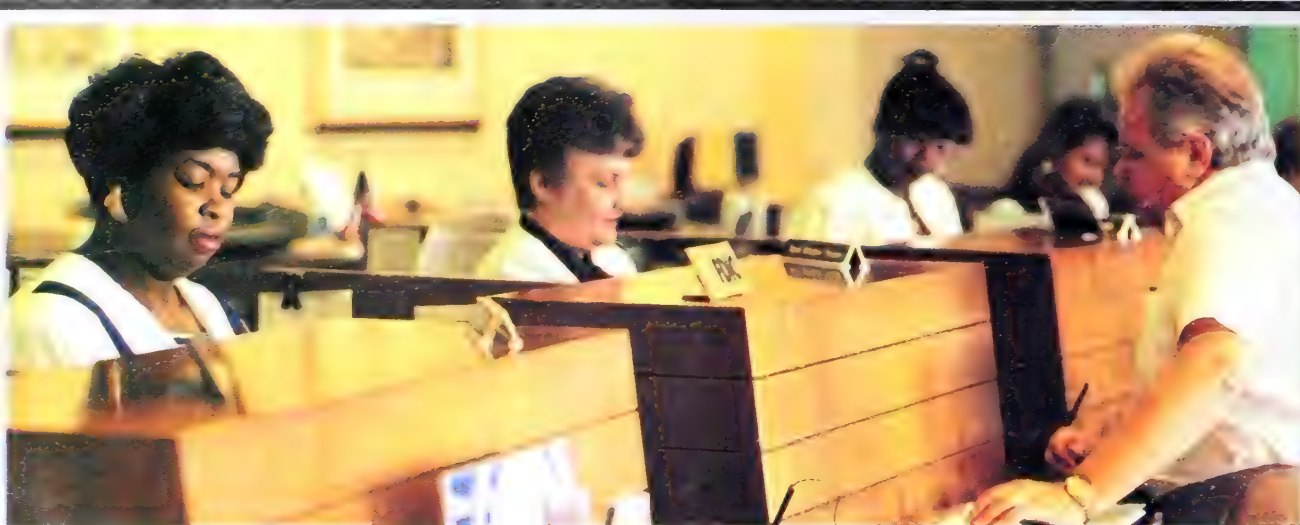
year tried unsuccessfully to broker a civil rights bill acceptable to both large corporations and minority activists.

Not every corporation functions on automatic pilot. Some highly visible companies, such as IBM, American Express, and Xerox, have embraced aggressive hiring and promotion programs for women and minorities (page 60). Although these models of equal opportunity cut across diverse fields, the key ingredient often seems to be a sustained top-down push from a chief executive. "Without commitment from a CEO," says Randall Kinder, a black senior vice-president at Equitable Financial Cos., "it just doesn't work."

Price Waterhouse is one firm where the message comes straight from the top. In 1989, as the accounting giant

was reeling from adverse publicity from an embarrassing sex-discrimination case, new CEO Shaun F. O'Malley set up an advisory committee on women and minorities. He invited prominent black accountants to serve on the panel. Then, "to make sure everyone knew how important it was, I made myself chairman." Adds O'Malley: "About 6% of our work force is black now. We want more. But more of the best."

In 1973, AT&T settled a landmark government discrimination suit by agreeing to hire and promote more minorities. The court order expired in 1979, but, with CEO Allen pushing hard, the company continues its aggressive recruiting of blacks. Today, minorities make up nearly 21% of AT&T's work force. And 17% of the company's managers



LIBERTY NATIONAL BANK'S MINORITY HIRES EXCEEDED THE LOCAL WORK FORCE PERCENTAGE—BUT FELL SHORT OF FEDERAL GUIDELINES

HOW THE RIGHT THING WENT AWRY

Following affirmative-action guidelines often looks easier than it is. Just ask Liberty National Bank & Trust Co. of Louisville. For years, it enjoyed a local reputation as a model equal-opportunity employer. Yet this April, it agreed to pay more than \$275,000 to avoid a federal discrimination lawsuit in what a Labor Dept. spokeswoman hailed as "one of the top 10 settlements nationwide this year."

Ironically, the problem arose, says Charles E. Allen III, the bank's attorney, "because of Liberty's long-term commitment to affirmative action and minority hiring." In 1989, Liberty hired 200 tellers and clerical workers; 16% of them were black. Since that number exceeds the percentage of minorities in the Louisville work force, the bank assumed that it was comfortable within federal guidelines. Not so, said the Labor Dept.'s Office of Federal Contract Compliance Programs. In a routine review of the bank's hiring practices, it discovered that 32% of the job applicants were black. So more of Liberty's hires should have been black. "If it weren't for the high percentage of [minority]

applications, there wouldn't have been a case," says Allen.

Among Liberty's 1,591 employees, 13% are black. Local civil rights officials confirm that the bank's track record in hiring is good—though they contend that, like other Louisville financial institutions, the bank still has too few blacks in upper-level positions. Minorities make up only 3.6% of bank officers, but that may soon change: Three of the 12 members in the management training program are black.

As part of its settlement with the government, Liberty will offer jobs to 18 of the minority applicants it turned down two years ago. Whether or not they accept, they will receive back pay equal to the amount they would have earned had they been working there since 1989—collectively, \$277,833. It could actually be less, since any wages they have earned from other jobs will be subtracted from their back-pay awards.

Liberty is also establishing a minority committee to advise on recruiting and retaining black employees—a move motivated, if not mandated, by the settlement. Apart from that, the bank plans no change in its affirmative-action efforts. Says Janet Geurin, the bank's black Equal Employment Opportunity Coordinator: "My feeling is we are making steady progress, and that's my benchmark."

By John Filatreau in Louisville

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are minorities, up from 12% in 1984.

AT&T also encourages its minority workers' participation in race-based support groups. These forums, which often have branches at every work site around the country, offer black managers a chance to share ideas, solve problems, and develop the networks white men have long relied on. AT&T's Black Managers' Group is one of 12 such affinity groups. All branches of the BMG, which was set up in the early '70s, meet twice a year for two-day conferences. Such race-based advocacy networks are increasingly common among progressive companies (page 53).

To get past the emotional charge carried by affirmative action, some employers have embraced a new catchphrase: managing diversity. Sometimes, this is to settle lawsuits. Northwest Airlines Inc. agreed to spend \$1.2 million on cultural-diversity training for all managers and to provide cash incentives for managers who meet minority hiring goals. Pillsbury Co. settled a class action, in part by agreeing to spend \$1.76 million to set up a "cultural diversity and training fund." The pro-

gram will, among other things, promote "ethnic cuisine and specialty events in the Pillsbury cafeteria."

Some of these earnest efforts can be easily lampooned. But many companies are serious about making their workplaces more congenial to minorities. Du Pont Chairman Edgar S. Woolard Jr. encourages workers to confront their biases in five-day workshops. The company also sponsored an all-expenses-paid conference for black managers to discuss how African-American culture can improve the company's bottom line. Managers who feel their heritage is valued are more productive, says one longtime Du Pont.

HARD TIMES. Yet plenty of corporations still duck the issue of hiring preferences. One large publisher based in the Midwest scrapped its voluntary affirmative-action plan when it failed to meet its own goals. What went wrong? A company official says it was lack of interest at the top. "There was no buy-in to the program," she says. "It's still a good-old-boy network."

Even the best of corporate intentions can be undone by economic hard times

(box). Take Equitable, the New York-based financial-services company. The firm spent years building its image among black managers as a "good" company. Now, after changing top management, Equitable is in the midst of a painful restructuring. Its black middle managers believe that affirmative action has been a casualty and worry that black advancement will suffer.

"We have maintained some semblance of affirmative action," says Darwen Davis, a black senior vice-president and 25-year Equitable veteran. But, he says, because of the company's "financial and internal problems, these are all back-burner issues." For example, the Black Officers' Council Davis used to head no longer meets. Equitable denies that it has reduced its commitment to affirmative action.

For other businesses, distaste for hiring blacks still exists. The owner of a small western Pennsylvania plastics company says he hired a black woman three years ago "to do the right thing." But after he passed her over for promotion, she sued, claiming race discrimination. The case is still in court, but the

A HARD CLIMB IN A DOWNTURN

The gleaming corporate offices of Hughes Aircraft Co. are just a few miles down the freeway from the gritty slums of south-central Los Angeles. David Barclay knows both worlds well. In the 1960s, he worked as a parole officer in Watts. Now, as a black vice-president in a company that once epitomized white male clubbiness, he is trying to pull those two worlds a bit closer.

Barclay, who joined Hughes in 1971, was named last year as vice-president for workplace diversity. His assignment: to come up with a program that would get minorities the top jobs that had so far eluded them. That would be a tough mission even in good times. But the defense industry is retrenching, and Hughes has eliminated 14,000 jobs in the past two years, with more cuts to come. Says Barclay: "We're doing all we can just to hold the line."

Today, minority employees make up one-third of Hughes's work force. That compares with only 13% 20 years ago. About 10% of the company's 51,000 workers are black. When it comes to the choice executive jobs, however, they still are rarely filled by minority employees.

BACKSLIDE. Part of the problem is a scarcity of minority professionals: Only 4% of Hughes's entry-level engineers are black, reflecting the relatively small pool of black engineers nationwide. But there is no such shortage of

Asians. They make up 24% of Hughes's 5,000 junior engineers—yet only one has risen as high as division head.

Barclay concedes that despite recent efforts, the Hughes corporate culture hasn't completely licked racism. "Not everyone is fully supportive of what we're trying to do," he says. And, while restructurings involving attrition and early retirements can often enhance minority opportunities, forced layoffs affecting less senior workers usually hurt. Hughes has not yet replaced most of the high-level women and minority executives who left. Just two years ago, the company had 12 women and minority vice-presidents, says Barclay. Today, there are 8 out of 92: two women, two Asians, two blacks, two Hispanics.

Hughes's cutbacks have forced Barclay to take the long view. He persuaded the defense contractor to provide about \$1.5 million worth of financial aid and lab equipment to seven black colleges in 1990. He has also launched an intern-

ship program that brings both students and faculty to Hughes to work with company scientists. And Barclay got Hughes to invest \$250,000 to help start a new mathematics and engineering public high school on the California State University campus at Domingus Hills, where most of the students are black.

These financial commitments are not huge. Still, "this is not a PR effort or window dressing," insists Barclay. "We are making a difference." The question is how much of a difference Barclay can make at Hughes while its business is shrinking.

By Eric Schine in Los Angeles



HUGHES'S BARCLAY: "THIS IS NOT A PR EFFORT"



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...of the...
...the payroll for years and has been fully satisfied with their work. But he says he will not actively recruit them. "It's not like it was in the old days," he says.

he appreciated it and didn't try to stir things up."

No CEO, surrounded by lawyers and affirmative-action advisers, would admit to such views. But some big companies have established practices that can end up being just as discriminatory. It's called hiring by the numbers.

Affirmative action is not supposed to be discriminatory with quotas. But virtu-

ally all companies doing business with the federal government must set annual plans, sometimes in the shape of numerical goals or timetables, for increasing employment of women and minorities. Companies often agree to meet specific hiring goals when they settle discrimination suits. In effect, quotas are prohibited and required at the same time—which can

MONSANTO'S NEW CHALLENGE: KEEPING MINORITY WORKERS

'W'e don't want quotas, and we don't need quotas," says Colton Isadore, a maintenance supervisor at Monsanto Co.'s Chocolate Bayou chemical complex in southeast Texas. The white backlash, he explains, "would really set things back." Isadore's opinion of quotas, while far from unique, is noteworthy for two reasons. First, Isadore's employer is one of affirmative action's most vigorous corporate champions. Second, Isadore is black.

Welcome to the complex—and sometimes contradictory—world of affirmative action at Monsanto. For more than a decade, the St. Louis-based maker of chemicals and drugs has focused on affirmative action to boost the number of minorities and women in its work force as both a federal requirement and moral duty. But management has discovered that simply dictating affirmative action in hiring alone can't change a corporate culture that has been long dominated by white men. So Monsanto, like Isadore, is searching for new ways to encourage workplace diversity beyond preaching the moral high road or playing on white male guilt.

Boosting the number of minorities and women in its traditionally white male chemicals subsidiary has been a priority at Monsanto since the 1970s: the company was awarded preferential hiring when the government came under heated assault by the Reagan Administration.

While a massive restructuring trimmed new hiring during the mid-1980s, the slimmed-down chemical company has generated affirmative action efforts in recent years. In 1988, 15% of nonunion new hires at the plant were minorities, 8% were women. In 1990, those percentages for minority and female recruits were 17% and 24% respectively. That compares with a

total division work force that is 11% nonwhite and 14% female.

But women and minorities were also quietly leaving Monsanto at a disproportionate rate. In 1988, 21% of the nonunion employees who voluntarily left the chemicals unit were women, 14% were minorities. By 1990, however, the percentages quitting women and minorities had jumped to 26% and 21%, respectively. "We were good at getting them in the front door, but just as quickly they were going out the back door, the back door, or any other way they could get out of here," recalls Michael E. Miller, Monsanto's corporate vice-president for administration. Now at corporate headquarters in St. Louis, Miller previously managed affirmative action for the chemicals unit.

DAMNING COMMENTS. The company began performing a series of detailed exit interviews and held focus groups with minorities and women who had voluntarily left its chemicals unit. In 100% of the minorities who had left said they wanted more responsibility and that they had experienced difficulty in dealing with their supervisors. Also, 30% more departed minorities than whites felt that Monsanto needs to give employees more help adjusting to new jobs. Furthermore, they felt treatment by their bosses seemed arbitrary and unfair.

The survey brought equally damning comments from departing women. Twenty percent more women than men said they were treated unfairly concerning pay and promotion decisions. And of the 40% women who had left, a huge 70% said their new employer offered greater opportunities for career advancement.

Top managers were puzzled that the employees felt left out of things. But it was no surprise to rank and file. "In the 1970s, we had low expectations for minorities," says Gerald Goodnight, technical services supervisor.



MONSANTO'S "CONSULTING PAIRS" INCREASE SENSITIVITY AND HELP REDUCE TENSIONS

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ake compliance a nightmare (page 56). Since the system encourages companies to focus on numbers of blacks on the payroll, rather than on individuals, companies face no penalty if their policies establish a revolving door, where a fixed percentage of black employees come and go, simply filling the same slots. Presto: instant compliance. "It can be difficult to get managers to move past the numbers," says William F. Holmes, vice-president at Em-

ployment Advisory Services Inc., a Washington consulting firm. "Everything they do is numbers. They have a production quota. Why not just have a human-resources quota?"

There is also some evidence that the current system may be setting a ceiling on minority hiring and promotion. Says Donald L. Huizenga, president of Larson Foundries in Grafton, Ohio: "We don't have to go out and hire minorities because our percentage [of minority

workers] is higher than the community of Grafton. If it weren't, we would be going out and recruiting." In nearly lily-white Grafton, 14% of Larson's work force is black or Hispanic.

Those blacks who make it into management ranks can find life lonely—and frustrating. Of 92 top management jobs at Hughes Aircraft Co., for example, only two are filled by blacks—the vice-presidents for communications and workplace diversity. "Rarely do I see a

Chocolate Bayou. "There was a lot of pressure to keep numbers up to meet our [affirmative-action] targets, and poor performers were carried. That kind of coddling is a barrier with other workers—a hell of a barrier. There were always a separate group that didn't get the feedback, the occasional kick in the tail they needed to develop. Eventually, a lot of them got tired of that treatment."

those who stayed often had to make personal adjustments. "I wasn't fitting in, so I started trying to act like a male," recalls Nora Castaneda, a Hispanic project-engineering supervisor at Chocolate Bayou. "I started dressing like I always made sure I had a comb sticking out of my back and I cussed up a storm—all of it in an effort to be accepted."

Experiences such as Castaneda's have led Chief Executive Officer Richard Mahoney to insist that Monsanto must go beyond affirmative action's emphasis on hiring. "At Monsanto, we must not force people to fight for their equal opportunities," says. "We must give it to them as a right."

That mandate, Monsanto began a series of managing-diversity programs, with Chocolate Bayou one of the key laboratories for the corporation's efforts. Almost more than 4,500 of the division's employees have undergone two-day diversity-training workshops, which help participants recognize often-unspoken assumptions and stereotypes about race and gender. During part of the training, employees are grouped anonymously to discuss the characteristics they believe are associated with different racial, ethnic, or gender groups. Those stereotypes are then displayed, and each employee publicly places a mark next to the one he or she agrees with—sparking sometimes-heated discussion about racial and sexual roles in the workplace.

A key element of the chemical unit's diversity effort is its "Joining Pairs" program, which trains employees from throughout the company to serve as in-house consultants (workforce or sex-matched pairs) on race and gender issues. For 3 days of intensive training, the pairs spend 10% to 20% of their work time for the next 18 months helping fellow employees cope with the challenges of life in a diverse work force. They also flag company policies, references, or even work assignments that may show racial or gender bias or stereotyping. Says David Scarr, a white operations-group leader who has been a pair-consultant: "When you have a teachable moment, you use it."

One of the pairs' key tasks is to conduct "join-up" sessions with new hires and their managers, as well as employees who are leaving jobs or managers. The sessions are structured to discuss expectations that both managers and employees have about

the new job—just the kind of give-and-take discussions that minorities and women who left Monsanto had complained they were not receiving.

NO SOP. But the pairs don't stop with the normal job formalities. They also push both employees and managers to talk about racial, gender, or age differences. "If they don't bring them up, then the pair is there to bring them up," explains Nancy L. Gheen, the chemical company's manager of work-force diversity. "They'll say something like, 'John, isn't this the first time you've had to report to a black man? How do you feel about it?' Once people begin to talk about these things, they're not as afraid of them and can learn to handle them."

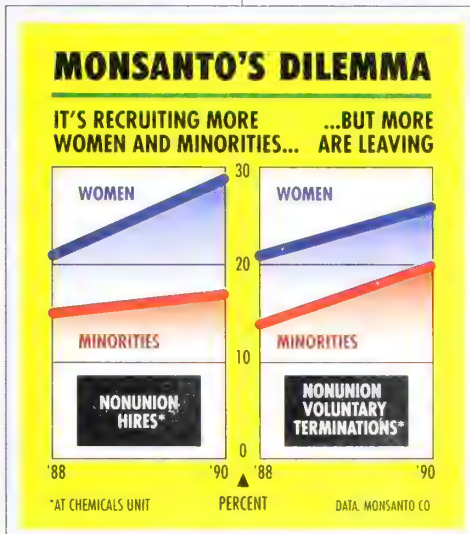
Monsanto officials readily admit that one of the key attractions of the Consulting Pairs program is that it serves the special needs of minorities and women without suffering the stigma of being a special-interest sop. Chocolate Bayou Purchasing Superintendent Rick Sharp crows that his join-up meeting with his new manager and two pairs "was a really good experience because we talked about things about my job and what we expect from each other that we just wouldn't have talked about before." Both Sharp and his manager are white men.

Using diversity programs to win the hearts and minds of people like Sharp is important—because white guilt doesn't sell the way it might have 25 years ago. Just ask William H. Slowikowski. The general manager of Monsanto Chemical's resins division admits "red flags go up in my head" whenever he hears the terms "affirmative action" or "equal opportunity." "I didn't personally do anything to get where we are today," he says. "I just happened to be born into a white family."

Yet now, Slowikowski heads the chemicals unit's Workforce Diversity Committee—a position he concedes he took with some skepticism. And after reviewing demographic forecasts, he's convinced that Monsanto must tear down racial and sexual barriers to remain competitive. "Recognizing the changing demographics shows that valuing diversity is good business sense—rather than something punitive that you've got to do for equal opportunity reasons to make up for something your predecessors did."

Diversity training is a slower approach than strict quotas to better the lot of nonwhite workers. But many Monsanto employees argue their approach is more in touch with the real world. "This isn't headquarters in St. Louis, where you can just impose solutions and then expect them to work," says Isadore, motioning toward the sprawling plant jutting above the Texas scrubland. "When it comes to managing diversity, this is where the rubber meets the road."

By James E. Ellis in Chocolate Bayou, Tex.



THE 'OTHER MINORITIES' DEMAND THEIR DUE

Listen to the noisy public debate about affirmative action, and you'd think the issue is entirely about hiring preferences for blacks. But the government's employment rules cover 48 million white women, 10 million Hispanics, and 3 million Asians in addition to 13 million blacks—in all, 54% of the labor force.

That makes affirmative action a tricky balancing act for the 225,000 companies that do business with the federal government. As competition in the labor markets intensifies, the "other minorities"—women, Hispanics, and Asian-Americans—are all insisting they should be considered first.

Of all the groups eligible for preferential hiring, women have fared the best. At 45% of the work force, they are hardly a minority—but affirmative-action laws cover them, because discrimination has kept so many in low-paying occupations. Women have, over the past 20 years, made enormous strides in corporations and, especially, in the professions: They now make up nearly 20% of lawyers, vs. 5% in 1970. "But there are still nearly 5 million women who work and live in poverty," says Cynthia Marano, director of Wider Opportunities for Women, an advocacy group in Washington.

Hispanics face a different set of problems. For many, language is a barrier to good jobs. So is employers' fear of hiring illegal immigrants. While affirmative action has "heightened the profile of Hispanics in the workplace," says Mario Moreno, director of the Washington office of the Mexican-American Legal Defense & Education Fund, "discrimination is still a critical problem." Hispanics make up 7.5% of the work force but hold only 4% of white-collar jobs. Instead, they tend to perform agricultural, janitorial, and other types of menial labor.

By contrast, Asian-Americans, 3% of the work force, face less resistance in getting hired for white-collar jobs. For

them, the need "is not just jobs—it's promotions, it's people moving into positions of power and authority," says Kathy Owyang Turner, acting director of Chinese for Affirmative Action in San Francisco. One of this group's unique problems: the widely held stereotype that Asian-Americans are hard workers but aren't assertive enough to be managers.

BOILING OVER. But the black, Hispanic, and Asian populations are all growing much faster than the white population. As a result, tensions among minorities are boiling over. "Blacks have been too successful at the expense of everyone else," grumbles Peter Roybal, a Mexican-American captain in the San Francisco Fire Dept. "Other groups have been ignored to placate the black community."

Such conflict is at its worst in California, where minorities make up 42% of the population. In Los Angeles, black and white members of Laborers Local 300 are suing to overturn a plan giving Hispanics preference in winning unskilled construction work. In increasingly Latino

Watts, the Martin Luther King Jr. Medical Center is caught between two groups: Hispanics want a bigger share of the health care jobs, but to accommodate them, the hospital would have to lay off the blacks who traditionally held these positions.

As competition for a limited number of jobs grows fiercer, affirmative action will almost certainly continue to pit one group against another. And employers are thrust into the uncomfortable role of deciding an issue the government won't touch: which minority is most deserving. Ask Larry Burnett, a white manager at Michigan Bell Telephone Co. He wants to promote a black male to a supervisor's job. But Burnett says his superiors are balking: "The personnel department says we are deficient in white females."

By Paula Dwyer in Washington, with Alice Z. Cuneo in San Francisco

THE CHANGING WORK FORCE			
PERCENT OF WORK FORCE			
1966	1980	1990	
WOMEN			
35.0%	42.0%	45.0%	
HISPANICS			
NA	5.6	7.5	
ASIANS			
NA	1.0	2.6	
BLACKS			
6.5	9.4	10.1	
NA=NOT AVAILABLE DATA: BUREAU OF LABOR STATISTICS; CENSUS BUREAU, BW ESTIMATES			

black man or woman with profit-and-loss responsibility," says Norman Hatter Jr., a black human-resources director for Du Pont's engineering staff. "That's where we really need to be."

Intellectuals such as Steele see an even deeper problem. In a collection of provocative essays on black-white relations, Steele writes: "One of the most troubling effects of racial preferences for blacks is a kind of demoralization, an enlargement of self-doubt." Even when blacks get a promotion, says University of Pennsylvania sociologist Elijah Anderson, they "run the risk of being seen as tokens. And that's a very difficult thing to handle."

The kind of hiring by the numbers that bothers Steele is just what angers many whites. Their anger doesn't seem to be based on personal experience, since, according to one recent poll, fewer than 1 in 10 whites say they have been victims of reverse discrimination. Still, when companies hire or promote blacks who are considered unqualified by their colleagues, it creates bitterness. "I question the factoring of affirmative action into hiring," says David J. Pandolfi, a white AT&T technician in Springfield, Mass. "It handicaps a company's future growth if an employer has to hire an unqualified individual in order to appease a politician."

Of course, "there are a lot of dumb white people who get breaks, and nobody seems too upset about that," notes William T. Coleman Jr., who as Transportation Secretary was the highest-ranking black in the Ford Administration. Still, Pandolfi expresses the feelings of millions of workers. It is understandable given affirmative action's legacy of racial tension, tokenism, and purely mechanistic compliance.

No question, the cost is high. But is affirmative action worth it? Yes. It's an important symbol of America's commitment to civil rights. More than that, it's an effective club. A deep vein of prejudice still runs through U.S. society, despite all the upbeat talk about the increasingly diversified work force. Government-mandated hiring preferences prod companies into integrating their work force, and in the past 25 years of affirmative action, blacks and other minorities have benefited socially and economically. Individual businesses and the economy have profited, not lost. Until America comes up with a better idea, it's wise to stick with a policy that, despite its flaws, is both a moral imperative and an economic necessity.

By Howard Gleckman, Tim Smart, and Paula Dwyer in Washington, Troy Segal in New York, Joseph Weber in Philadelphia, and bureau reports

CORPORATE AMERICA GRADES ITS EFFORTS

Corporate executives insist they don't need anyone twisting their arms to hire more women and minorities. A hefty 65% of those polled insist that business will open up its hiring and promotion practices without affirmative-action laws. That may be because Corporate America feels that the marketplace is already forcing companies to end discrimination in employment. Executives point to the shifting com-



position of the labor supply and the benefits of a diverse work force as bigger spurs to affirmative action than fears of government or private lawsuits.

Even so, more than half say their companies need to do a better job of hiring minorities, and 44% aren't satisfied with their progress in hiring women. Another weakness: failure to promote women and minorities into top management.

MORE LEGISLATION PROBABLY ISN'T NEEDED

■ Do you feel that there should be affirmative-action laws on the hiring of women and minorities, or do you think most companies such as yours would hire and train and give women and minorities the opportunities to get ahead without such laws?

Need affirmative-action laws	31%
Business will do the job itself	65%
Not sure	4%

COMPANIES ARE AGGRESSIVELY RECRUITING MINORITIES

■ In the hiring of women and minorities, does your company do any of the following, or not?

	Does	Does not	Not sure
Set numerical goals but not quotas for hiring them	40%	48%	12%
Make special efforts to recruit them	78%	17%	5%
Use lower hiring standards for them	5%	88%	7%
Offer special in-house training programs for them	34%	60%	6%

THE DRIVING FORCE? A LABOR SUPPLY IN FLUX

■ Among companies you know, do you think each of the following is very important, somewhat important, not very important, or not important at all in increasing their hiring of women and minorities?

	Very important	Somewhat important	Not very important	Not at all	Not sure
The fear of private lawsuits	20%	42%	29%	7%	2%
The benefit of having different types of people in the work force	50%	36%	9%	2%	3%
The worry about government enforcement action	26%	45%	21%	5%	3%
The changing makeup of the labor supply	52%	36%	6%	2%	4%

BUSINESS COULD BE DOING MORE FOR MINORITIES

■ Do you feel your company needs to do a better job of hiring, training, and promotion of minorities, or not?

Needs to do a better job	53%
Does not need to do a better job	42%
Not sure	5%

... AND COULD IMPROVE ITS TREATMENT OF WOMEN

■ Do you feel your company needs to do a better job of hiring, training, and promotion of women, or not?

Needs to do a better job	44%
Does not need to do a better job	52%
Not sure	4%

OVERALL, COMPANIES ARE DOING AN O. K. JOB . . .

■ How would you rate the track record of companies such as yours on each of the following—excellent, pretty good, only fair, or poor?

	Excellent	Pretty good	Only fair	Poor	Not sure
Hiring women and minorities into entry-level jobs	29%	57%	12%	0%	2%
Promoting women and minorities into middle management	20%	48%	27%	3%	2%
Promoting women and minorities into top management	8%	22%	44%	23%	3%
Retaining women and minorities	25%	50%	13%	1%	11%

... AND WITHOUT HUGE HEADACHES

■ How much trouble do you feel this whole area of affirmative action has caused your company—a lot of trouble, some but not a lot, or not much trouble?

A lot of trouble	6%
Some but not a lot	39%
Not much trouble	53%
Not sure	2%

Edited by Mark N. Vamos and Christopher Power

Survey of 404 senior executives at corporations drawn from the BUSINESS WEEK 1000. Interviews were conducted June 10-14, 1991, for BUSINESS WEEK by Louis Harris & Associates Inc.

**TO ALL OF YOU
WHO SAID
WE'D NEVER BE
ON THE
SAME LEVEL
WITH THE
BIG COMPUTER
MAKERS.**

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4. Hewlett-Packard
5. Everex
6. CompuAdd
6. Compaq
8. Epson
9. Toshiba
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WHAT'S IN A NAME? LESS AND LESS

Mad Ave. worries that familiar brands may be losing their punch

When Robert L. James calls on clients these days, it's not just to press the flesh. The blunt-speaking chairman of ad agency McCann-Erickson Worldwide is sounding a tocsin: Brand names, he says, are in trouble. Companies aren't spending enough to support these valuable assets. As a result, the products that carry them are losing their premium status. What's more, James thinks that few marketers fully appreciate the threat: "I feel like I'm screaming in a void."

With a client roster that includes Coca-Cola, RJR Nabisco, and General Motors, James seems an odd person to fret about the durability of brand names. His agency helped Coke sustain its unshakable bond with consumers by drumming into them that Coke is the real thing.

MAKING THE SWITCH. Nobody would deny that the payoff from such advertising is huge: Mass marketers have enjoyed a reliable stream of profits at home and abroad. Owning strong brands has allowed them to price their products at a premium. Indeed, the top-selling brands have undergone remarkably little change in ranking over decades (table).

So why is James acting like Paul Revere? Because he worries that marketers are letting brands slip away. Retailers have been forcing companies to divert dollars from advertising for their products into costly trade promotions, such as payments for space on store shelves. That dims the prominence of brand names. Also, advertising is no longer as effective, because the decline of mass media has made it harder to hammer home a single, coherent message. The net effect: Brands are being devalued. They aren't disappearing, James says, but consumers are more willing to switch to cheaper products.

Two recent studies bear out his fears. A survey by DDB Needham Worldwide Inc. found that 62% of consumers polled in 1990 say they buy only well-known brand names, compared with 77% in 1975. A Grey Advertising Inc. study says 61% of consumers regard brand names as an assurance of quality—a drop of six percentage points since July,

1989. In the same study, 66% say they are trading down to lower-priced brands. And almost half are buying more store or generic brands.

But suggest that brands are declining to many marketing executives, and you'll get staunch disagreement. "Brands are becoming more important than ever," says Herbert M. Baum, president of Campbell Soup Co.'s North American operations. Baum is spending millions on ads to revive such brand icons as the Campbell Kids. "The brand is the most important thing in marketing," agrees David J. Gustin, marketing chief for Frito-Lay Inc. Frito's parent company, PepsiCo Inc., continues to advertise heavily, while other big marketers are retrenching. Indeed, PepsiCo made the power of brands the theme of its latest annual report.

How can James be so worried when top marketers say they are sanguine? One reason is self-interest. As marketers put more money into coupons and other promotions, they're reducing their support of the big-budget ad campaigns that generate much of Madison Avenue's profits and prestige. Advertisers spent 70% of their marketing dollars on consumer and trade promotions in 1990, leaving just 30% for ads. Advertising's share has been dropping steadily since

SHELF LIFE

Here are some of the most durable brand names, with their market rank in 1923 and today:

Category	Leading brand in 1923	Current rank
Cameras	KODAK	No. 1
Canned fruit	DEL MONTE	No. 1
Chewing gum	WRIGLEY'S	No. 1
Crackers	NABISCO	No. 1
Razors	GILLETTE	No. 1
Soft drinks	COCA-COLA	No. 1
Soap	IVORY	No. 1
Soup	CAMPBELL	No. 1
Toothpaste	COLGATE	No. 2

DATA: BOSTON CONSULTING GROUP



Donnelley Marketing began tracking these expenditures in 1978.

Yet even marketing experts with no vested interest in fat ad budgets say companies are neglecting their brands. "The marketing community is in the process of destroying the meaning of the brand," says Al Ries, chairman of Trout & Ries, a marketing firm in Greenwich, Conn. As a result, consumers are starting to regard many brands as interchangeable: "People don't think the world will come to a screeching halt if they use Tide instead of Cheer," says Joel D. Weiner, former marketing chief of Kraft General Foods Inc.

STEADY STREAM. Weiner and others say the issue is more complicated than simple ad dollars. For one thing, marketers are relentlessly extending their brands. Because companies want to produce a steady stream of new products to fill shelves and fuel sales growth, many are slapping their established brand names on a broad range of new products.

Sometimes this works well, such as when Procter & Gamble Co. rolled out Tide With Bleach in 1988. But line extensions have drawbacks. In 1979, for example, Miller High Life was a strong No. 2 beer brand after Budweiser, sell-



say they are developing innovative ways to extend their product lines. One method is to establish new brands that aren't identified with individual products. Historically, brand names were rooted in concrete product attributes: Colgate toothpaste prevents cavities.

Now, however, companies are coining brands that appeal to a type of lifestyle. For example, Con-Agra Inc. recently began marketing a line of frozen dinners to health-conscious shoppers under the brand name Healthy Choice. It also sells breakfast baked goods, egg substitute, and even ice cream under that name. Marketing experts say that type of stretching works because it doesn't rely on a core product for its appeal. Another method is to double up brand names. Campbell now sells Mrs. Paul's frozen fish

filets made with Pepperidge Farm breeding. Baum argues that the two brand identities set the product apart from rivals without weakening the image of either brand.

WAX AND WANE. Despite the lure of line extensions, there is evidence that some marketers are shying away. Campbell plans to introduce fewer new flavors and products in the 1990s—after a heady period in the late 1980s, when it rolled out 214 new products. After years of declining budgets, Campbell will boost ad spending 30% next year. P&G, after cutting back on ad spending as a percentage of sales in 1989, increased its ad budget 24% in fiscal 1990. Chairman Edwin L. Artzt has said that ad spending in the U.S. will grow again this year.

Brands wax and wane slowly. It took years for once-powerful monikers such as Pepsodent toothpaste and Oxydol laundry detergent to become marketing ciphers. So it will take at least a decade to determine whether brands are really in trouble. Still, it's not too soon for marketers to start worrying about their good names.

By Mark Landler in New York, with Zachary Schiller in Cleveland and Lois Therrien in Chicago

g more than million barrels a year. But once Miller Brewing Co. introduced Miller Lite and Miller Genuine Draft, the core brand languished. High Life now sells 6.4 million barrels, compared with Budweiser's 10 million barrels. High Life was also hurt by a price hike in 1980. But the new brands only made matters worse.

Such examples haven't deterred marketers. Of the 6,125 new products placed on shelves in the first five months of 1991, just 5% bore new brand names, according to *Gorman's New Product News*. The rest are variations on existing brands: Tropicana Twister Light fruit juices, Huggies baby wipes, and the like. **BLEACH BLANKET.** Marketers also lean on line extensions because of the enormous risks in introducing a new product. Roughly 9 out of 10 new brands fail, according to marketers, and a mistake can cost dearly. Clorox Co. spent \$225 million to develop a new line of laundry detergents. But it couldn't persuade enough shoppers to buy detergent from a company famous for bleach. Clorox retreated from the category in May.

As if that weren't enough, ad executives say, many brand managers don't see much need to nurture brands. Quick

turnover leads them to focus too much on short-term sales objectives. Ad execs also fault business schools for training MBAs to care more about numbers than less tangible brand assets. Roy Bostock, chairman of D'Arcy Masius Benton & Bowles Inc. and himself a Harvard MBA, says young brand managers "lack the capacity to grasp the concept of brand equity." Marketing consultant Larry Light is less diplomatic: He says MBA stands for "Murderer of Brand Assets."

The end result, say marketing Cassandras, is that the power of leading brands will slowly fade. Secondary brands face an even dimmer future: Because they are less profitable and require more advertising support than leading brands, many will shrivel and be supplanted by store or generic brands. A survey by A.C. Nielsen Co. says consumers already spend 14.2% of their total grocery dollars on private-label brands.

Still, many investors cling to their belief in brands. Kohlberg Kravis Roberts & Co. paid some \$30 billion to take over RJR Nabisco Inc. in 1989 based largely on the strength of names such as Camel cigarettes and Ritz crackers. To avoid diluting such valuable assets, marketers

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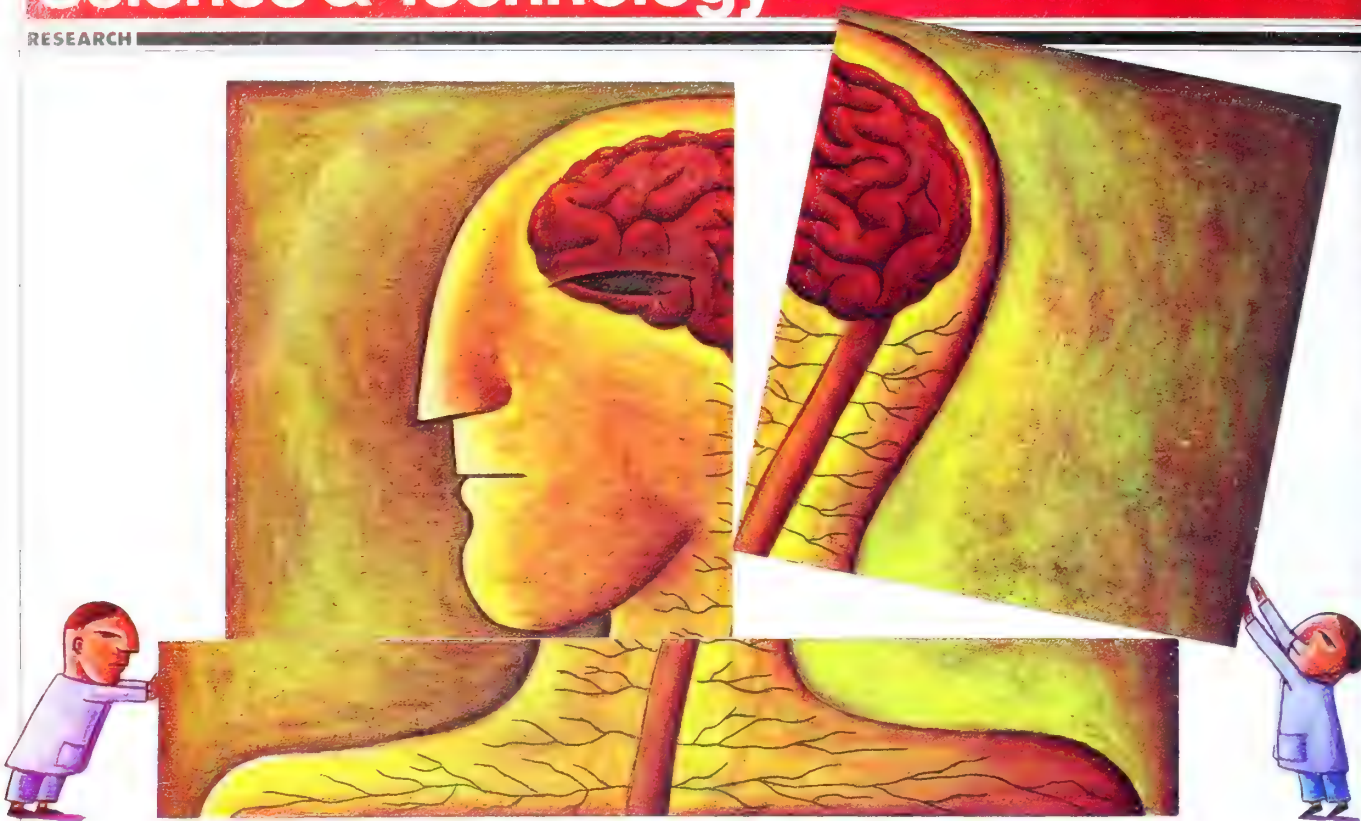
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HOW DO YOU MEND A BROKEN BRAIN?

Science is making strides in stemming nerve-cell damage

In August, 1986, John Breeding, then 23, took his pickup out for a spin along the dirt roads of rural Delaware. Racing around a corner, he hit a drainpipe at the side of the road and flipped over into a ditch. With his head caught between a partially open window and the truck's roof, his neck snapped. When paramedics arrived, Breeding had no feeling from his neck down—he was effectively a quadriplegic.

Two days later, at the Shock Trauma Center at the Maryland Institute for Emergency Medical Services in Baltimore, Dr. Fred H. Geisler began treating him with an experimental drug called GM-1. The results were startling: After two months, "I started feeling my toes," says Breeding. And from then on, he began regaining motion. Now, his left side is nearly normal, and he has some function in his right arm and leg. With a brace he can walk, drive, swim, and "even mow the lawn," he says. "If I hadn't gotten the drug, I would have

been paralyzed from the neck down."

Just a year ago, there was only anecdotal evidence that any drug could help prevent paralysis caused by spinal-cord injuries. But last May, researchers announced a new use for an old drug called methylprednisolone: It can limit damage when given within the first few hours after a spinal-cord injury. And now, in a study headed by Geisler that appeared in the June 27 issue of *The New England Journal of Medicine*, GM-1, made by Fidia Pharmaceutical Corp. in Italy, was shown to significantly enhance the recovery of half of the 16 patients receiving the drug. Like Breeding, most of those were able to function much better than untreated patients just six months after being injured. "For the first time, we've been able to move neurological recovery from the laboratory into clinical practice," says Geisler, chief of neurology at the Columbia Medical Group in Columbia, Md.

Perhaps even more striking, the same

drugs that are showing such promise in spinal-cord injury are also being investigated—along with a half-dozen others—to treat stroke and head injuries. That's potentially a much larger market. Only 10,000 Americans suffer spinal-cord injuries each year, but nearly 400,000 suffer strokes, the third-largest killer in the U.S. An additional half-million incur serious head injuries in accidents. The market for a drug that would treat such problems is estimated at upwards of \$2 billion a year in the U.S. alone. In addition, there is evidence that some of these drugs may also be helpful in halting the progression of such degenerative ailments as Alzheimer's and Parkinson's disease. "It's becoming very clear to drug companies that there is a halo effect," says Dr. Wise Young, director of the neurosurgical laboratory at New York University Medical School. "Drugs for use in the spinal-cord area can be extended to other diseases."

OVEREXCITED. The reason may be that, in all cases of injury to the central nervous system, the original trauma causes the death of cells in only one defined area. With a stroke, for example, the damage is caused by a blood clot or a bursting blood vessel—called an aneurysm—that shuts off the blood supply to an area of the brain. Affected cells die within a matter of minutes. But the damage doesn't stop there. As these original neurons, or brain cells, die, they

leash a chemical cascade that radiates outward like a nuclear explosion, eventually killing millions, if not billions, of neighboring nerve cells. "All of the injury that occurs with trauma is not immediate but expands over a day or two later," says Richard P. Bunge, director of the University of Miami's Project to Cure Paralysis. So far, science can do little to avoid the damage that occurs in the first few minutes after a stroke or injury. But drug companies are looking for remedies that would intervene in the delayed reaction and block much of the long-term damage to nerve cells.

The first step is to understand exactly what happens after the original trauma. Dr. Dennis W. Choi, head of the neurology department at Washington University in St. Louis, thinks that so-called excitotoxins play a major role in the damage. After a stroke or brain injury, he says, dying brain cells release massive amounts of a chemical called glutamate. Normally, glutamate is a key player in long-term memory and learning. But the brain functions under a very sensitive chemical balance, and too much glutamate is toxic. When the glutamate reaches weakened cell membranes, it causes "calcium channels" to open, allowing calcium to flood the cell. The effects of this flood are twofold: "overexcites" the cell, stimulating the production of enzymes that ultimately lead to self-destruction. And the calcium triggers the release of more glutamate, so the chain reaction continues to spread to neighboring cells.

CHEMICAL COCKTAIL. One approach to stemming this destruction would be to use drugs that block the receptors, or docking sites, for glutamate on cell membranes. That would prevent the calcium channels from opening. Several large pharmaceutical companies, including Hoffmann-La Roche Inc. and Ciba-Geigy Corp., already have such drugs in early clinical trials for the treatment of stroke. Unfortunately, these drugs are relatives of the street drug called angel dust, which can cause some temporary—but serious—psychiatric problems.

By contrast, Fidia's GM-1, one of a class of naturally occurring compounds called gangliosides, seems to have few side effects. That's because, unlike the other drugs, it may block just those calcium channels involved in cell damage. Now, a few biotech companies, including Cambridge Neuroscience in Cambridge,

Mass., and Neurex in Menlo Park, Calif., are working on even more precise ways to target the specific glutamate receptors that open the channels.

Still other companies are pinpointing different steps in this glutamate cascade. Neurotherapeutics, a San Diego startup, is trying to stop injured nerve cells from releasing glutamate in the first place. And Cortex Pharmaceuticals Inc., in Irvine, Calif., is working on inhibiting some of the damaging effects of calcium once it enters the cell. Calcium activates an enzyme called calpain that normally helps establish long-term memory. But when a flood of calcium is re-

leased into the cell, it acts as a switch, causing calpain to go haywire and destroy the cell from the inside out. Now, Cortex has developed a drug that—in animals—blocks this action.

NEW DRUGS FOR VICTIMS OF STROKE OR BRAIN INJURIES

Much of the damage to the central nervous system from a stroke or an injury to the brain or spinal cord is caused by toxic chemicals produced by the body itself. Now, researchers at several companies are testing new drugs that can block the effects of these chemicals—and thus prevent paralysis and other complications

GLUTAMATE-CASCADE BLOCKERS

CIBA-GEIGY, HOFFMANN-LA ROCHE, MERCK, CORTEX, CAMBRIDGE NEUROSCIENCE, NEUREX, NEUROTHERAPEUTICS

After an injury, dying nerve cells release massive amounts of a brain chemical called glutamate. This sets off a chain reaction that overexcites neighboring nerve cells, eventually killing them. Some of these drugs, which are now in the experimental stage, would protect surrounding cells by blocking the receptors for glutamate on their membranes. Others would interfere with another step, the influx of calcium into the cells

LAZAROLDS

UPJOHN After trauma, nerve-cell membranes also come under attack from so-called free radicals—charged oxygen molecules. The lazardoid drugs dissolve into the cell membranes and protect them from free-radical damage

GANGLIOSIDES

FIDIA Gangliosides are proteins that are found in the membranes of nerve cells. They are believed to block calcium activity and may help stimulate nerve growth and repair. In recent experiments, injections of the proteins helped reduce paralysis caused by spinal-cord injuries

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leased into the cell, it acts as a switch, causing calpain to go haywire and destroy the cell from the inside out. Now, Cortex has developed a drug that—in animals—blocks this action.

According to Choi, the treatment of choice for stroke or brain injuries will probably include several of these drugs, a chemical cocktail of sorts. That's because glutamate isn't the only culprit in nerve-cell damage. In their swan song, dying cells also release large amounts of so-called free radicals. These are charged oxygen molecules that break down the fat particles that make up cell membranes. This makes the membranes leaky, again letting calcium flood the

cell. Methylprednisolone, a generic drug that's now being used to treat spinal-cord patients, seems to infiltrate these cell membranes and help protect against free radicals. But because this drug is a steroid, it has some undesirable side effects—including suppression of the immune system.

BIGGER MIRACLES. In another approach, Upjohn Co. has discovered a whole new class of drugs, called lazardoids, that also lodge themselves in nerve-cell membranes and protect them from free radicals. One compound, tirilazade, has already been tested in people who have serious head injuries, and NYU's Young says it is "about a hundred times more potent than methylprednisolone and at the same time, it has no side effects." John M. McCall, executive director of discovery research at Upjohn, says lazardoids may also hold promise for strokes, and the company has started clinical trials to test them.

As researchers learn more about how to block the chemicals that cause the devastating damage from trauma and stroke, they are also getting hints about how to treat the long-term degeneration caused by Alzheimer's and Parkinson's disease. That's because the end result of trauma and neurodegenerative diseases is the same, says Young—"the loss of nerve cells." One theory about the cause of Alzheimer's, for example, is that glutamate and other excitotoxins may cause a slight, but chronic, overexcitement of the nerve cells, says Dr. Fred Gage, professor of neuroscience at the University of California in San Diego. The long-term effect could be to weaken these cells, making them vulnerable to other damage. In fact, says Upjohn's McCall, there is evidence that the brain of a person with

Alzheimer's may be more sensitive than a normal person's to free radicals. For that reason, the company is trying to develop a lazardoid that could be tested against Alzheimer's—and even aging.

Researchers are eyeing even bigger miracles: They talk eventually of coaxing injured nerve cells to regenerate. In the meantime, there's plenty of work to do on trying to prevent central nervous system damage. "We've known about stroke for three centuries and still don't have a treatment," Choi says. Now, John Breeding is living proof that science is at long last making progress toward solving such problems.

By Naomi Freundlich in New York

FICHE & CHIPS.



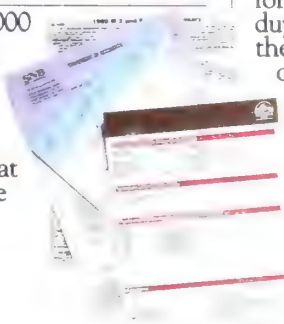
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THE IMAGE OF THE FUTURE.
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Developments to Watch

EDITED BY WILLIAM D. MARBACH

FROM PUTT-PUTT TO VROOM! WITH THE TURN OF A KEY



Want to turn your stodgy car into a hot rod? Adaptive Technologies, a Port Hueneme (Calif.) company, has designed a system that lets you select the computer chip controlling your engine. Until now, speed freaks who wanted to tweak their engines had to crawl under the dash to swap the carmaker's engine computer for one that boosts

power by altering the air-fuel ratio and the spark timing. The new system, which costs \$219, fits most General Motors Corp. cars and trucks built since 1984 and holds up to four different engine-controller chips. Adaptive says it takes 30 minutes to install, then all you do for more oomph is turn a key in the dash. You can choose a chip that gives you more power when you want it—or one that provides better fuel economy. Another can be a security chip that foils thieves by disabling your car's fuel and electrical systems. You can even choose one that limits engine power and then remove the key, so the kids can't get too wild on the way to the store.

TESTING STEEL ALLOYS WHILE THEY'RE STILL IN THE FURNACE

To make high-quality alloys, steelmakers test each batch by drawing a sample of molten metal, then taking it to the analyst's lab. There the sample has to be heated in a vacuum chamber so the vapors can be analyzed. At Pennsylvania's Lehigh University, Professor Yong Kim has patented a method for testing molten metal directly inside the furnace.

The LPP (laser-produced plasma) Sensor Probe unit fires a laser beam into the molten metal, causing some to vaporize. A computer then analyzes the plasma's spectrum to determine the alloy's composition. All this takes less than a minute, compared with up to 10 minutes for the conventional test.

By reducing waste and cutting the time molten metal must be heated in the furnace, the new process could save the industry as much as \$200 million a year. The Lehigh project is funded partly by the federal government and an industry consortium that includes the American Iron & Steel Institute. Initially, the apparatus should cost between \$300,000 and \$1 million, depending on the size of the plant.

SHORTCUT TO A PROMISING CANCER DRUG

One of the bright hopes in cancer research is the discovery that taxol, a compound derived from yew trees, is effective against ovarian cancer, a disease that kills 12,000 women in the U.S. alone each year. The drug also shows promise in treating breast, lung, and colon cancer. But supplies are very scarce, because taxol is made from the bark of the Pacific yew tree, a relatively rare, slow-growing species found only in the old-growth forests of the Pacific Northwest.

Unfortunately, taxol's carbon-ring chemical structure is difficult to synthesize. Now, two small biotechnology companies, Phyton Catalytic Inc. in Ithaca, N.Y., and ESCAgenetics Corp. in San Carlos, Calif., may have a better solution. Independently, the companies are developing fermentation processes that will coax cells of the yew tree to produce taxol in a bioreactor, similar to the way yeast makes alcohol.

Phyton has an exclusive license from the Agriculture Dept. to use its tissue-culture technology to produce taxol and similar compounds and has already tested the process in the lab. The next step: full-scale production systems, a process that could take two to five years, says Rustin R. Howard, Phyton's president. ESCAgenetics officials say their process has also been proven in lab tests—and should be ready for commercial production within the next two years.

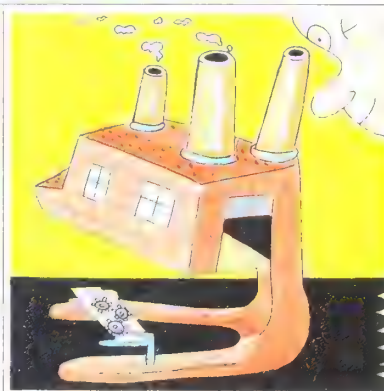
THIS ELECTRIC-CAR BATTERY REFILLS LIKE A GAS TANK

Someday soon, drivers pulling into a service station to "fill 'er up" might want battery fuel, not gasoline. Luz Industries Ltd., an Israeli solar-energy company, has developed a refuelable battery for electric cars. Forget about overnight recharging, says Yehuda Harats, president of the Jerusalem-based Luz Electric Fuel subsidiary: The battery's 20 gallons of zinc-based slurry, which generates electricity by reacting with oxygen in the air, would be drained and replenished in about five minutes.

Each fill-up would last for about 300 miles, and the depleted slurry would be collected by the oil companies, recharged, and then resold at their filling stations. Early next year, Luz plans to demonstrate its battery with a 400-mile spin around California, then kick off production in 1994. Initially, the refuelable battery will be expensive—roughly \$10,000—but the company expects the price to drop to around \$2,500 with volume production.

MICROMACHINES ARE GETTING SOME REAL MUSCLE

Scientists are making microscopic gears, turbines, and other components of micromachines—tiny motorized systems that might one day be built into semiconductors or placed inside the human body. But many of the efforts involve silicon components so thin they can't generate much torque. Yet, fashioning thicker metal microstructures



often requires exotic and expensive equipment—such as X-ray synchrotrons—available only to a few top labs.

Georgia Institute of Technology electrical engineer Mark G. Allen has an alternative. Allen's group uses conventional microelectronic lithography to etch gear patterns into a common plastic. These molds are filled with copper or nickel. So far, the group has created metal gears about 300 microns wide and 50 microns thick—a human hair is 100 microns in diameter. Allen says the gears should have enough torque for many uses—such as in motors that could help precisely position fiber-optic lines into telecommunications chips.

THE INSIDER-TRADING COPS WIDEN THEIR DRAGNET

Now, regulators and legislators are focusing on abuses in all securities markets—not just stocks



Last October, a Franklin County (Ky.) Circuit Court grand jury accused Noble Donald Morse II and his father, Donald Morse, of a popular crime: insider trading. But unlike Ivan F. Boesky and Dennis B. Levine, who dealt in stocks, the Morses face the novel charge that they “misused confidential information” to trade state bonds.

The younger Morse, who was then secretary and treasurer of Kentucky’s Infrastructure Authority, allegedly tipped off his father about the agency’s plans to buy back some 1973 bonds on Aug. 1, 1990. The redemption plans were made known to a select group of investment firms that the agency had contacted for help in setting the buy-back price. The Morses bought \$110,000 in bonds in July, allegedly expecting that the state would redeem them at a higher price.

The maneuver turned a quick \$6,000 profit. The Morses have pleaded innocent. Says J. Guthrie True, Donald’s at-

torney: “None of the information Morse used was confidential.”

Innocent or guilty of the charges, the Morses could well earn a spot in the history of securities law for having been defendants in the first insider-trading case involving municipal bonds. Their case, moreover, is just part of a broad—and unprecedented—campaign by regulators and other law-enforcement authorities on information abuses in markets for securities other than equities. “There is a bit of a shift going on in our focus,” says Securities & Exchange Commission Chairman Richard C. Breen. “We are likely to give greater attention to the various debt markets.”

LITTLE OVERSIGHT. The result could be new insider-trading laws and broad disclosure rules in markets that historically have operated with little regulatory oversight and something of an anything-goes culture. A lot is at stake. The \$3.3 trillion government-securities market is

one of the world’s largest, about the size of the stock market. Municipal and junk bonds, respectively, have some \$840 billion and \$230 billion outstanding.

When Congress wrote the securities laws 50 years ago, most of the attention was on stock abuses. No one much worried about the sleepy markets for corporate bonds and government or municipal debt. Commodity trading was but an agricultural sideshow, and financial futures didn’t exist.

Now, trading in nonequity markets is exploding. As it has become riskier and more volatile, so has the opportunity to trade profitably on privileged information. The key reason is that there is little required disclosure of information about issuers or of trading data, such as price. Issuers, traders, and others often have a big edge over the public.

Insider-trading laws cover all securities, but so far have been applied mostly to stocks. Corporate executives and di-

etors who trade on inside information are usually prosecuted for breaching their fiduciary duty to shareholders. But they have no such duty to bondholders. Insider traders are usually accused of "misappropriating," or stealing, company information. Yet that theory hasn't been applied by courts to debt traders. Although commodities trading is heavily regulated, there are no direct prohibitions against insider trading, which is widely regarded as integral to commodities markets.

The government hopes to change all this. The SEC is looking into debt abuses, especially in the junk-bond market. Congress is exploring insider-trading laws for commodities. These efforts will likely lead to much more disclosure, which could narrow the yawning gap between information haves and have-nots.

Perhaps the most visible problems, as regulators see it, are in the market for junk bonds. They often trade like stocks, rising or falling on news about the issuers. The SEC has made the junk market "greatest concern," says Breeden. His goals include boosting disclosure and making junk prices more available.

'SHING.' Breeden also wants to nab insider traders. The SEC's New York regional office is conducting what it terms an "informal inquiry" into trading by members of creditor committees involved in negotiating debt restructurings for troubled, often bankrupt companies. The SEC apparently believes that

some committee members may have traded on information about these negotiations, which often affect the price of outstanding bonds. One lawyer for a firm questioned by the SEC calls the effort "a fishing expedition."

The SEC is also probing investors who buy bank loans made to troubled companies. By buying such debt, the investors often gain access to the companies' confidential information. The SEC suspects some investors use this data to trade in the companies' junk bonds.

Junk-bond prices are also affected by takeover negotiations, just as stock prices often are. Junk-bond price runups just before bullish announcements are confirmed by "lots of studies," says Professor Donald C. Langevoort of Vanderbilt University School of Law. On Jan. 1, for example, Harcourt Brace Jovanovich Inc. accepted a \$1.4 billion takeover

bid from General Cinema Corp. But on Jan. 23, HJB's 13% bonds jumped \$50. The bid has since expired.

The information trickle to junk bondholders is a flood compared to the data flow to municipal bondholders. Unlike corporate debt, muni issuers are exempt from the SEC's financial-reporting rules. Much of the disclosure burden falls on bond trustees, who are supposed to represent bondholders. In practice, the trustees' allegiance sometimes lies with issuers, who pay their fees.

The once-placid muni market has acquired junklike turbulence as credit ratings plunge for deficit-ridden issuers, such as Philadelphia and New York. Many small issuers have defaulted: Bridgeport, Conn., even filed for bankruptcy. The result? "Opportunity for some market participants to adjust their positions ahead of the investing public;

firm claimed that it "completely disclosed the essential facts and risks."

Rising muni defaults and bondholder demands are forcing changes. Bond industry groups are working on guidelines that spell out the trustees' disclosure duties. The SEC and the Municipal Securities Rulemaking Board, a self-regulatory group, are implementing plans to make public more data about muni issuers.

OPEN BOOKS. Momentum for a level playing field is even building in the huge U.S. government-securities market. Primary dealers in Treasuries and interdealer brokers have long enjoyed exclusive access to trading data. And because they trade directly with the Federal Reserve, primary dealers can often sense shifts in Fed policies that affect interest rates. Representative Edward J. Markey (D-Mass.) is circulating a bill that, among other things, would empower the

SEC to make brokers and dealers open their price quotes to the general public. The threat of legislation has the slow-paced industry scrambling to launch market-data services.

The biggest challenge for regulators lies in the futures markets, where traders often use nonpublic information to hedge or speculate on future commodities prices. Such trading is not only widely accepted but also considered essential. In part because of the widely publicized commodities scandals, Congress is mulling legislation banning some forms of insider trading in commodities. A Senate bill

would bar trading on knowledge gleaned through work on an exchange board or committee. More fearsome to the industry is a House bill that would cover many more forms of insider trading.

"What the House is trying to do sounds good, but it freezes the flow of information that the whole marketplace depends on," says Thomas E. Neal, a Chicago trader. But CFTC Commissioner Fowler C. West disagrees: Insider trading "is just as wrong in futures as it is in securities."

Other regulators have similar views about their own markets. The transition to fairer, more open markets for debt and futures won't be easy. But cracking down on alleged transgressors such as the Morges may be needed for the markets' continuing growth.

By Michele Galen in New York, with Dean Foust in Washington, D. C.

POLICING ABUSES BEYOND STOCKS

JUNK BONDS

The Securities & Exchange Commission is probing possible insider trading in the high-yield debt market. Market regulators are mulling whether to mandate more disclosure and more price information to bondholders

COMMODITIES AND FUTURES

A Senate bill would make it a crime for trading on inside information gleaned through work on an exchange governing board or committee. A House bill would prohibit a much broader range of insider trading abuses

MUNICIPAL BONDS

The Attorney General of Kentucky last October brought what is apparently the first insider-trading case involving municipal bonds. Concerned about rising defaults and the dearth of information to small muni investors, the SEC and such industry groups as the Municipal Securities Rulemaking Board have initiated sweeping disclosure rules

DATA BW

GOVERNMENT SECURITIES

Responding to a General Accounting Office report last year alleging abuses, a House subcommittee is considering a bill to empower the SEC to oversee brokers and dealers in the \$3.3 trillion government market. It would also mandate broader dissemination of price data. In reaction, industry groups are scrambling to launch market data services

in other words, to trade on inside information," says Los Angeles bond lawyer Karen J. Hedlund.

Nancy and Theodore D. O'Hearn would probably agree. In mid-1989, the couple spent \$80,000 on hospital-revenue bonds sold by Choate-Symmes Health Services Inc. in Arlington, Mass. They bought the bonds from a local office of Minneapolis-based brokerage Dougherty, Dawkins, Strand & Yost Inc. In a lawsuit, the O'Hearns and others allege that the firm and two brokers were trumpeting the bonds even though they knew the hospital was financially sick. The suit alleges that the firm was simply unloading its inventory of the bonds before Choate went belly-up.

Dougherty responds that the public had plenty of red flags, including Standard & Poor's Corp.'s credit downgrading of the bonds from A- to BB. The

Commentary/by Larry Light

LETTING THE AIR OUT OF INSURERS' OVERBLOWN ASSETS

Insurance companies these days are collapsing in droves. Yet Nostradamus himself would have a hard time predicting the next to go belly-up. For mere consumers, anxious about policies they've bought to fund retirement or to support their families after they die, divining an insurance company's well-being is well-nigh impossible.

The problem: Insurers are allowed to carry most of their investments at cost. A bond bought for \$1,000 is booked at par even though it may get only \$500 in the market. While Executive Life Insurance Co. listed \$10 billion in assets at the end of 1990, much of that was junk bonds, and the market value was less. In April, regulators seized Executive Life and its affiliates. The biggest insurance failure ever, it stranded thousands of policyholders.

So let's rip away insurers' accounting fiction that assets never vary in price. Let's compel them to mark their assets to present market values. The industry should be required to mark to market—say, once a quarter—and send the results to policyholders, who would have a better idea of what they've bought. Potential buyers should get those results from salespeople.

THINKING TWICE. With that knowledge, clients of Executive Life and First Capital Life Insurance Co., another recent insurance failure, could have tracked the plummeting bonds that backed their policies—and compared them with those of sturdier rivals (chart). With market pricing, insurers would think twice about risky investments. Mutual funds—long-term vehicles like life insurance—already mark to market. If the thrifts had followed those principles, their debacle could have been contained. Asks Harold D. Skipper, director of Georgia State University's Center for Risk Management & Insurance Research: "Why insulate people from bad news?"

Consumers can't turn to regulators for help. The data state insurance departments provide are skimpy. Worse, regulators are often too lax and under-staffed to detect ailing insurers until

it's too late. California officials should have seized Executive Life long ago. Congress may beef up insurance oversight by imposing federal standards. But history's sad lesson is that regulatory zeal ebbs with the political tides.

Another insolvency spotter to view warily is A. M. Best Co., whose ratings books are available in local libraries. The books' information is often a year old, and Best can be overly lenient. Until recently, Executive Life carried Best's second-highest rating, which is well within the safety zone. Best defends its approach as sound and blames Executive Life's demise on sudden and unforeseen public panic that caused a flood of policy redemptions.

In practical terms, marking to mar-

issuers send in. A formula could be doped out, using the agency's data base, to pin values to them, too.

Valuing real estate, whose woes have zapped insurers far worse than junk bonds, is the toughest challenge. Property values are a kaleidoscope involving such variables as location and building type. Nonetheless, requiring insurers to make yearly appraisals and compile vacancy and debt-load information could yield workable numbers.

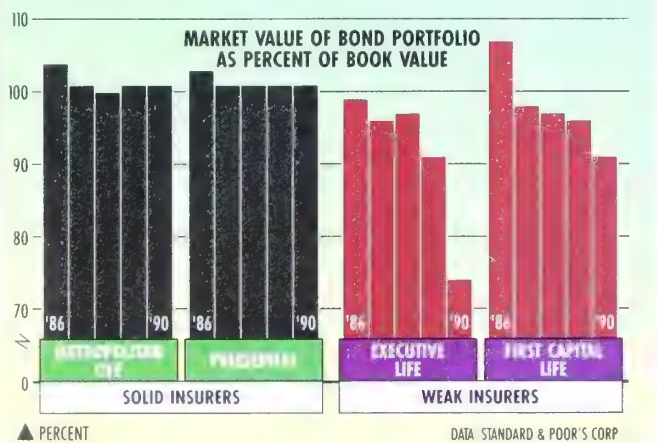
VOLATILITY. Insurers greet the idea of marking to market like an invitation to a Russian roulette party. They argue that many of the liabilities the assets support—death benefits and annuity payouts—won't come due for a long time, so why worry about temporary fluctuations? Says Linda S. Dougherty, vice-president for accounting at Prudential Insurance Co.: "This would mislead and scare people." But the vast majority of insurers don't have to worry about spooking policyholders. Typically, they are very conservative investors with Gibraltar-like stability. The value of Pru's bonds has stayed steady for years.

A more valid industry fear is extreme market volatility, such as during the late 1970s, when interest rates shot up and bond prices sank. Then, even Pru's portfolio would take a beating. Still, there's a remedy: Mandate that insurers

bolster capital to fill the gap between liabilities and diminished assets. The riskier the insurer's holdings, the more capital it should have.

Pricing to market is no theorist's pipe dream. Securities & Exchange Commission Chairman Richard C. Breeden backs it. The Financial Accounting Standards Board (FASB) may soon require insurers, banks, and other institutions to disclose market information as an appendix in filings. Anticipating this, several regional banks such as Atlanta's Suntrust Banks Inc. are preparing to make market-price asset disclosures. The FASB next will examine applying market values to the balance sheets. Good. Caveat emptor is useless when disclosure is empty.

HOW MARKET PRICING SEPARATES THE FIT FROM THE FAILING



ket is not as hard as it seems. Bonds, which make up more than half of the average insurance investment portfolio, are easy to value because most are publicly traded. Insurance providers already tally bonds' market value at yearend for state regulators. On balance sheets, they have long market-priced their stocks, foreclosed mortgages, and defaulted bonds.

Valuing the rest of the portfolio will be harder, but not impossible. Consider private placements, direct investments in companies that do not trade in public markets. The Securities Valuation Office of the National Association of Insurance Commissioners assigns risk ratings to thousands of private placements, on the basis of information the

Quick, do you know
the first name
in microprocessors?

_____ 486™

_____ 386

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THE BIG BOARD'S BIG YAWN

Almost everyone finds the NYSE's after-hours system too limited

When the New York Stock Exchange commenced after-hours trading on June 13, many a brow was furrowed on Wall Street. Some observers expressed concern that the new system would hide trading data from public view and undermine the Big Board's links with regional exchanges. But the naysayers have had little reason to complain—not because the system is working well, but because hardly anyone is using it.

The NYSE's nascent effort to compete with institutional trading systems and overseas exchanges has aroused barely a ripple of interest from either the public or institutions. When trading began on June 13, 737,000 individual shares were traded, plus 1.6 million stock-basket shares (in units of 15 or more different stocks). But individual shares traded have dropped by two-thirds, with no stock baskets traded on some days (chart).

MATCHMAKING. At brokerages and money-management firms alike, the reaction has been tepid. Discount giant Charles Schwab & Co. reports that just 30 to 50 customers a day—out of 1.5 million—are using the NYSE after-hours system. Another major discount, Fidelity Investments, has found customer interest to be nil and did not begin to accept orders for after-hours trading until June 24. And even firms that have used the system from the beginning have found it disappointing. At Merrill Lynch & Co., which strongly supports after-hours trading, the Big Board's system has attracted only a scattering of orders and even fewer have been executed. The managing director for listed-equity trading, Robert J. McCann, notes that except for some stock-basket trades, "we have not had a significant transaction in the after-hours trading system so far."

The poor results are a depressing omen for the NYSE, which

has geared up its after-hours foray, on a two-year trial basis, to win back business from order-matching systems such as the Crossing Network and POSIT, and from the London and Tokyo exchanges. Through 1993, the exchange will have two daily after-hours sessions, with one session matching buyers with sellers of individual stocks at the 4 p.m. closing price from 4:15 to 5 p.m., Eastern time. The other session permits trading of stock baskets through 5:15 p.m. for insti-

tutions that want to reshuffle portfolio

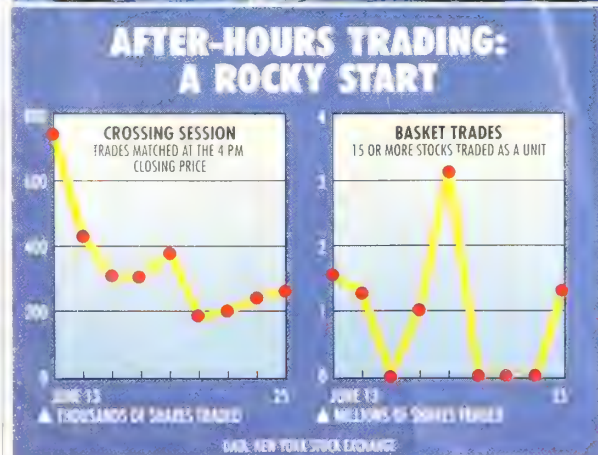
From the beginning, the NYSE system has evoked criticism. For one thing, it's a limited order-matching operation—trades are executed only if there are buyers and sellers at the closing price. Moreover, some critics have maintained that the matching session undercuts the Intermarket Trading System, which links the NYSE with regional exchanges, because the trading only takes place at the NYSE. The basket session has come under fire because trading data on individual stocks is not disclosed.

LOST CAUSE? The most glaring shortcoming of the NYSE system appears to be that trades can only take place at the closing price. It's a downside not present at POSIT or the overseas exchanges. Usually, only a fraction of match-trading orders can be filled. At one major brokerage, large-block orders totaling 30,000 shares a day were entered into the NYSE system on June 13 and 14—but only about 500 shares a day were traded. "After that," an executive of the firm recalls, "we just didn't bother"—and stopped using the NYSE system. The Teachers Insurance & Annuity Association-College Retirement Equities Fund had a much better initial experience—with 40% of its orders filled on June 13. But the percentage has since dropped to about 3%. The "fill rate" for TIAA-CREF trades placed through Instinet, by contrast, is as high as 15% for large-cap stocks.

For its part, the NYSE is downplaying the sparseness of the volume and the rate of order execution. "If it's an up day and everybody is entering buy orders, people are not going to be matched," notes spokesperson Sharon Gamsin, who contends that reaction to the system has been positive.

But the exchange will not release the overall fill rate of customer orders. And until that number—whatever it is—increases and volume picks up, big customers will stay away. "People are sitting on the sidelines, so there's no volume, so we're sitting on the sidelines," notes Michael Even, a senior vice-president of Independence Investment Associates in Boston. "It's a chicken-and-egg thing." Indeed, the egg may never hatch. Says a top trader at one major brokerage: "It is a nonevent. In a month, nobody will even be talking about it."

By Gary Weiss in New York



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BY GENE G. MARCIAL

WHY THE SLIDE IN HIGH TECH HASN'T TOUCHED SCITEX

With technology stocks on the ropes, Scitex should be reeling by now. But the maker of computer-aided-design systems for automated image reproduction hasn't slumped. In fact, Scitex has continued to rise even though Chairman Robert Maxwell (of publishing fame) and a group of Israeli investors have reduced their combined stake from 51% to 47%.

What's shoring up Scitex? For one thing, several pros are grabbing shares sold by Scitex insiders. "Scitex remains a home-run stock," insists money manager Paul Wick of J. & W. Seligman. He thinks Scitex, now at \$30 a share, is worth \$50.

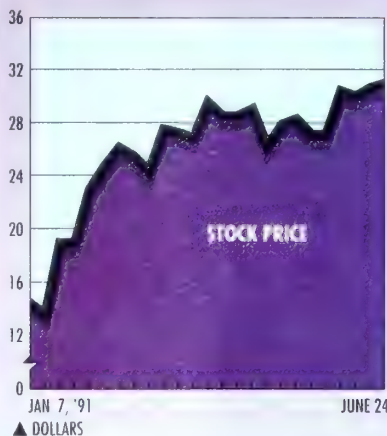
Moreover, orders for its hardware and software from both the U.S. and Europe continue to increase despite the recession. Scitex, whose turnkey computer-imaging systems are used mainly in publishing and graphic arts, has "outscored its competitors in revenue growth and order backlog," says Wick.

Analyst Alex Henderson of Prudential Securities sees a "solid potential for upside earnings surprises." In recent years, Scitex has exceeded analysts' earnings and sales expectations. And Henderson says it's likely that earnings will again exceed his estimates: 63¢ for this year's second quarter, \$2.60 for all of 1991, and \$2.90 for 1992. Last year, Scitex earned \$2.10.

RICHER PALETTE. One source of expected growth: Scitex' new midrange products, which make color printing more affordable for small companies. This fast-growing market, which added sales of \$20 million to last year's revenues, is expected to contribute \$100 million in three years. Scitex already controls 50% of the high-end market, where rivals include Crosfield, owned jointly by Du Pont and Fuji Photo.

Don't worry about the insider selling, says Henderson. Maxwell, chairman of Britain's Mirror Group, assumed the chairman's post at Scitex in January, 1989, when he invested \$39 million for a 27% stake. He isn't selling because of any disappointment over the company's performance. Rather, he needs cash to meet financial obligations, in part because of his recent purchase of the financially strapped *New York Daily News*.

SCITEX: STILL ON THE RISE



DATA: BRIDGE INFORMATION SYSTEMS INC.

The Israeli group includes PEC Israel Economic, Cial Electronic Industries, and Discount Investment. Henderson says the group's usual strategy is to invest in small, emerging growth companies. But with revenues projected to hit nearly \$400 million this year and earnings increasing robustly since 1987, Scitex is growing, all right, but 'small' and 'emerging' no longer apply.

QUAKER'S FANS KEEP THE FAITH

Quaker State traded as high as \$31 a share in 1987, but it has been more or less on the skids since then. Now, it sells at just a shade below its book value of \$11 a share. The company, which produces motor oil and operates a chain of quick-lube centers, has been struggling to boost earnings, which fell 40% in the first quarter. But that hasn't spooked such big investors as Mario Gabelli, who holds a 8.2% stake. Indeed, other pros have been buying, too. Why?

"There are two ways to win with Quaker State," says investment pro George Clairmont. "As an earnings turnaround and as an asset-value play." Clairmont, president of Clairvest, notes that with the stock near its lowest multiple in 10 years, Quaker is "one of the cheapest stocks around." Based on assets, he puts the company's breakup value at \$20 a share.

Clairmont doesn't see an imminent buyout, even though Quaker was a rumored takeover stock in the '80s. But he believes Quaker is exploring the sale of its insurance and coal units, which Clairmont thinks have a com-

bined worth of \$11 a share. "At the stock's current price," he argues, "you're buying the core lube businesses for nothing."

Quaker's Heritage Insurance has turned profitable, but its Valley Camp Coal has been a loser—in the red by \$1.3 million in the first quarter. The Truck-Lite unit, which makes safety lighting for trucks and cars, also posted a big loss in the first quarter.

But Clairmont sees an earnings recovery in the second half. Although profits for 1991 will be flat, he expects a jump to \$1 next year, vs. last year's 72¢. Meanwhile, "you're paid a 7% dividend yield to wait for the stock to rise," says Clairmont. A Quaker spokesman says management is looking closely at its coal operations.

CLEANING UP IN TOXIC CLEANUP?

No, Harding Associates isn't a marketing or PR firm. It's in toxic-waste cleanup—a hot investment since the late '80s. But this year, interest has waned, in part because the recession has crimped spending on waste cleanup. Even so, Harding has attracted some big investors, among them Neuberger & Berman, which is rumored to have a 4% stake.

The stock, which trades over the counter, has fallen to 13, down from its high of 25, and the company has warned that earnings for the year ended May 31 declined slightly from last year's 96¢ a share. Still, says money manager Steve Leeb, president of Money Growth Management: "The stock is a rare bargain that's too good to pass up." He thinks earnings will recover smartly later this year. Leeb says the stock is selling at only about 10 times his \$1.20-a-share estimate for 1992, and it's way below the price-earnings ratios of other waste-management stocks, such as Allwaste and Chambers Development. Plus, Harding is debt-free.

Since 1986, revenues have more than tripled, to \$69 million, and earnings have leaped eightfold. Leeb says the growth stems from Harding's start-to-finish services. Unlike rivals, which specialize in particular areas of waste management, Harding tackles everything from initial-site inspection to full cleanup. It also designs disposal facilities for hazardous and solid waste.

What's more, insists Leeb, the industry's giants have taken notice: "Harding is the next takeover stock in the waste business."

Some like it hot.



L. WYSE LURZER

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TESTING, TESTING: MORTON AND ITS NEW PARTNER, GERMANY'S BOSCH, ULTIMATELY HOPE TO GRAB THE LION'S SHARE OF EUROPE'S MARKET

STRATEGIES

WILL AIR BAGS CUSHION THE NEW MORTON?

It plans to invest \$600 million, but the payoff is way down the road

When Morton Thiokol Inc. spun off its aeronautics business in mid-1989, Chairman Charles S. Locke hoped to take his company on a profitable new course—one free of painful associations. After all, a faulty booster rocket made by Morton Thiokol triggered the 1986 Challenger space-shuttle explosion and marred the outlook for the once-thriving aeronautics unit. Now, both the business and the Thiokol name have been jettisoned. But that leaves the refashioned Morton International Inc. decidedly earthbound. It is dominated by a clutch of slow-growing businesses in salt and specialty chemicals.

So how can Morton soar again? Locke thinks he has found the answer: air bags for automobiles. Since jumping into the field during the early 1980s, Morton has captured some 55% of the \$400 million global air-bag market, which is expected to grow fourfold by 1995. But while the business shows promise, it has perils, too. Competition is heating up both here and abroad, and the technology is expensive and fast-changing. What's more, Morton will invest hundreds of millions through the mid-1990s to develop its air-bag business before seeing much in the way of returns.

HEADING EAST. Undeterred, Locke is expanding Morton's position on several fronts. In the U.S., Morton is now the sole air-bag supplier to Chrysler Corp., and it recently picked up Ford Motor Co. as a customer. Morton is also quickly making its presence felt in Europe. In mid-June, Morton and Germany's Robert Bosch announced plans to jointly devel-

op an air-bag venture to serve the European car market. "We've got to get our feet wet [overseas]," says Locke.

If Locke sounds like a man in a hurry, it's not hard to fathom why. With air bags expected to be a standard safety feature on most U.S. and foreign cars by the mid-1990s, the market should enjoy explosive growth for some time to come. So far, air bags are little more than a trifle to Morton: It earned \$15.3 million from air-bag sales of \$163 million last year. But Locke expects Morton's air bags to be a \$1.3 billion business, or 30% of total revenues, by 1995. And that potential has investors panting: Morton's stock has jumped 25% this year, to about 55—more than twice the run-up for Standard & Poor's 500-stock index.

But even Locke admits that Morton's air-bag gambit could spring a leak. The company plans to pump \$600 million into the business by 1994, but the earnings payoff will probably be slow in coming. Right now, profits in Morton's air-bag operation are about half of the 15% to 20% return-on-invested-capital goal that Locke has in mind for the unit. In fact, the company will probably have to wait until 1996 before sales grow large enough to provide a decent return. "The

return on capital is pretty lousy," says Locke. "It's going to get even lousier before we're through."

That's too bad, because Morton could use a little lift. Its \$1.02 billion specialty-chemicals business has been hobbled by the recession. And demand for its specialty polymers, coatings, and sealants has been hammered by the severe downturn in the auto and housing markets. Meanwhile, a string of relatively mild winters has zapped sales of Morton's road-salt products, slowing growth of its \$450 million salt business. The glacial performance of its core units has dampened Morton's financial outlook. For the fiscal year ending July 31, it is expected to post a paltry 2.5% earnings gain, to \$138.2 million, on \$1.9 billion in sales.

PROMISING LINK. Small wonder, then, that Morton is elbowing its way into air

bags. Its European link with electronics giant Bosch looks particularly promising. Morton boasts a sophisticated air-bag technology that involves the electronic triggering of a controlled explosion of the chemical sodium azide. That, in turn, generates hot gas that inflates the air bag in a fraction of a second. Morton's edge: Drawing from its experience in rocket propulsion, the

company's former Thiokol unit developed a reliable production method for the air bags—a task that has bedeviled competitors.

Bosch will bring to the party an expertise in crash sensors and diagnostics, the triggers for air-bag detonations. The partners ultimately hope to grab the lion's share of Europe's still-tiny air-bag business, but it may be a while before that market grows much. With seat-belt use running at an impressive 90% in Europe, drivers may feel no



...pelling need to pay for air bags. To help nurture demand, Morton and Bosch plan to do a fair amount of lobbying in Brussels. The European Community is considering legislation that would mandate the use of air bags in all new automobiles by 1994. And Bosch has a reputation for knowing which strings to pull. "Bosch is politically smart," says Dan Lewis, a joint-venture consultant based in Washington. "They know how to influence things."

BATTLEFIELD. Still, Morton will face decidedly stiffer competition in Europe than it did in the U.S., where it was long the first to develop a reliable air bag. Other companies, such as Germany's Siemens and Sweden's Electrolux Autoliv, already supply air-bag components to many European carmakers and plan to start assembling the devices soon. In September, Electrolux Autoliv started supplying air-bag systems for Volvo-Scania cars exported to the U.S. And Japanese carmakers, armed with air bags from Takata Corp., are trying to lure more cars in Europe, posing another direct threat to Morton's overseas ambitions. "In air bags, Europe is going to be more of a competitive battlefield than Japan or the U.S.," says Andrew Flowe, a consultant with SRI International in London.

Stateside, Morton will continue to battle off against Cleveland-based TRW, its primary rival in air bags. So far, Morton holds sway. TRW's system has been plagued by production-line fires as well as quality problems, both of which the company now claims it has solved. Admittedly, the technology is tricky to master. Last year, Ford had to recall more than 165,000 cars and cancel an exclusive supply arrangement after TRW air bags leaked hot gasses into passenger compartments. That's one reason TRW has yet to turn a profit on its air-bag business.

TRW isn't conceding the European market to Morton, however. The Cleveland company will push its current air-bag products, while focusing on a new-generation product that uses argon gas, a cheaper alternative to chemical mixes, which it hopes to have on the market by the mid-1990s. If TRW's advances come on line in time, say TRW executives, the Morton-Bosch alliance will still be beaten. Says Adolph Mueller, vice-president and general manager for TRW's occupant-restraints group: "I would be concerned with somebody who is in the business with only one technology."

For now, though, it looks as if Morton is getting ready to benefit from the coming air-bag bonanza. If so, air bags could be quite a boost for a company that likes to leave some unpleasant recent history light-years behind.

By David Greising in Chicago

STRATEGIES

NEWELL ISN'T BAGGING BIG GAME ANYMORE

Two buyout bids are stalled—and Stanley looks out of reach

Sure, Newell Co.'s products—the likes of pots, pans, and curtain rods—are mundane. But its profits have been the stuff of dreams: Thanks to a long string of acquisitions, the obscure houseware and hardware manufacturer has churned out an average annual profit gain of 26.5% since 1976, with net income reaching \$101.3 million last year. Meanwhile, revenues have soared to \$1.1 billion from just \$87 million. And unlike many deal-hungry companies, Newell has financed its purchases out of cash flow, so its balance sheet is virtually debt-free.

But Newell's growth engine may be running low on gas. The company hasn't made a major acquisition since it bought glassware maker Anchor Hocking Corp. for \$350 million in 1987, a move that doubled revenues, to \$988 million, the following year. Newell, based in Freeport, Ill., has purchased a few companies, each with some \$50 million in sales, since then, but it has been rebuffed in its last two attempts to buy larger corporations. Although it delivered a 19% earnings increase last year, the slowdown in acquisitions hit the top line: Revenues fell 4.5%, the first dip in more than a decade. The recession hurt, too, as the weak housing market reduced demand for Newell's kitchen and window hardware products.

To get its growth chugging again, Newell is now chasing its biggest deal yet. In June, it sought antitrust approval from the federal government to buy up to 15% of \$2 billion hardware maker Stanley Works. The venerable New England company responded by setting up takeover defenses and by filing an antitrust lawsuit against its acquisitive suitor. Newell Chief Executive Daniel C. Ferguson insists he will continue to court Stanley. "I've done this for 25 years," says 63-year-old

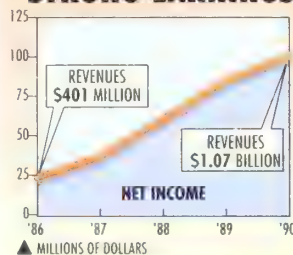


CEO FERGUSON: "WE'LL GROW WITH OUR CUSTOMERS"

Ferguson, whose father was one of four Newell founders back in 1921. "We've got time."

But time is no guarantee that Newell's investment will bring Stanley, based in New Britain, Conn., into the fold. Newell has long been the master of what one target calls the "creeping takeover." It acquires a small stake in a target company and then opens merger negotiations. But this strategy worked better before the Anchor Hocking deal raised Newell's profile. "People have their antennae up looking for Newell," says one competitor. Indeed, despite two years of wooing, Newell hasn't been able to creep above its current 10.1% stake in hair-care

NEWELL DISHES UP STRONG EARNINGS



goods manufacturer Goody Products Inc. or its 5% of glassware maker Lancaster Colony Corp.

Stanley would be a big gulp for Newell. Although debt stood at just 16% of Newell's total capital at the end of 1990, the company had only \$20 million in cash at the end of the first quarter. A deal for Stanley could top \$1.5 billion, and loans for highly leveraged deals aren't exactly easy to come by right now. Ferguson says he would consider swapping 20% of Newell for 20% of Stanley, but a Stanley spokesman says the company wants to remain independent.

Fortunately, dealmaking is only half the Newell story. The company owes part of its success to Ferguson's decision in the late 1970s to focus on selling to mass-market retailers such as Wal-Mart Stores, K mart, and Home Depot. As those companies experienced explosive growth during the 1980s, Newell grew with them.

LITTLE TOUCHES. Distribution and service became Newell hallmarks. In the late 1970s, the company was among the first in its industry to establish electronic links with its customers. That enabled retailers such as Wal-Mart to order goods via computer instead of through the mail or by telephone. And the company doesn't forget the little touches. Its employees often restock shelves for retailers, freeing up store personnel for other tasks, says K mart Corp. Division Sales Manager Wayne Sales.

Newell has proved adept at integrating new companies into its system. After buying Anchor Hocking, Ferguson split the company into units centered on product lines, closed a money-losing glassware factory in West Virginia, and lopped \$60 million off overhead. Anchor's consumer glass business was losing \$10 million on revenues of \$200 million when Newell bought it, says Ferguson. Last year, it posted a 15% net operating margin.

Newell's steady stream of acquisitions has paid off for shareholders, too. Since 1983, there have been three 2-for-1 stock splits. Newell was trading at 35 recently, up from about 6 shortly after the October, 1987, stock market crash. Since insiders own roughly 15% of the company, management has profited nicely from its rapid growth.

Ferguson insists that Newell can thrive without making another big acquisition. "We'll grow with our customers and rely on new products," he insists. In the works, for example, is a tamper-proof seal for baby-food containers that could generate annual sales of up to \$30 million. But unless Ferguson lands Stanley or one of his other targets, the Newell earnings machine may be stuck in lower gear for a while.

By Kevin Kelly in Chicago

Information Processing



PERIPHERALS

QUANTUM HAS ONE TOUGH HURDLE TO LEAP

Shrinking PC sales may slow the disk-drive maker's rebound

When Stephen M. Berkley took over as chairman of computer hard disk-drive maker Quantum Corp. in 1987, he knew he was in for a tough slog. For three years, sales had been mired at about \$120 million. And because it was late with its new generation of drives—ones with 3½-inch platters instead of 5¼-inch—Quantum had lost all but two of its customers. When the drives finally came out in 1988,

the market was glutted and prices were crashing. "We had to do something pretty dramatic," Berkley recalls.

He did, and it worked. Thanks to unique development and manufacturing strategies—and the coattails of its biggest customer, Apple Computer Inc.—the Milpitas (Calif.) company is now the fastest-growing drive maker. In fiscal 1991, ended Mar. 31, sales hit \$878 million, making it No. 3 behind Seagate Technology Inc. and Conner Inc. Says Dataquest Inc. analyst J. Philip Devin: "Quantum is the company to watch."

Actually, that's not hard, since most of its competitors are fal-

tering. Because of slow personal-computer sales, the market for hard-disk drives is growing by just 8%, to \$18.3 billion—one-third of the 1990 rate. Maxtor Corp. lost \$50 million in its most recent quarter, as prices for some drives plunged 50%. Conner Inc., a superstar startup, last quarter saw sales drop 10% from the preceding one, to \$382 million. PrairieTek, based in Longmont, Colo., just laid off 210 of 325 employees.

STOCK DROP. So far, Quantum has fared better. But Berkley says revenues will decline quarter-to-quarter into the fall. And Apple, which accounts for 41% of Quantum's sales, recently signed IBM to supply some drives. Meanwhile, Quantum plans to launch five new products this year, twice the usual number. All this has pushed Quantum's stock down to 11, from nearly 18 in April.

This difficult season should show whether Quantum's success resulted from Berkley's strategies or simply from being on Apple's team when it was on a tear. Since Berkley and David A. Brown, Quantum's





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president, took charge, Quantum has plotted an unusual course. In manufacturing, for instance, it follows neither Seagate nor Conner. Conner buys rather than builds most of its components, thereby avoiding high fixed costs. But when demand jumps, as recently happened in its 2½-inch line, it can run short of parts. Seagate, by contrast, makes many components so it can gear up production quickly to earn high profits when demand is strong. But when demand slows, its large fixed costs hurt.

Quantum used to be like Seagate. But in 1983, Berkley and Brown launched a new subsidiary to build the Hardcard, a 3½-inch disk drive on a circuit card that snaps into an IBM PC. To build it quickly, they enlisted Japan's Matsushita Koto-buki Electronics Industries Ltd. MKE had never made a disk drive, but as the world's largest maker of videocassette recorders, it had proven skills in making electromechanical gear. It was a risky move because it could produce a strong Japanese competitor in hard disks. But so far, the gamble has paid off. By 1987, Hardcards were contributing 54% of Quantum's sales and all of its profits.

With development of Quantum's other

products bogged down, Berkley and Brown took the reins of the whole company. They hired MKE to speed Quantum's push into 3½-inch drives. MKE made Quantum revamp the way it develops drives, insisting they be designed with robotic assembly in mind. Some drives had to be redesigned 30 times. "After four months, our engineers were ready to quit," Berkley recalls.

But Quantum got the benefits of building in-house—without the cost. MKE plowed about \$150 million into automated plants. So, 97% of the drives leaving MKE's assembly lines need no reworking, compared with 90% or less for most competitors. That gives Quantum among the highest gross margins in the industry, even after MKE's cut.

NEW TEAMS. Lately, Berkley and Brown have focused on development. Disk-drive product generations had shrunk to less than two years, but development was still taking up to three. They set up teams for each product line, which were free to draft needed talent from engineering, sales, marketing, finance, and other departments. For Quantum's 2½-inch drives, due out this summer, designers came up with final specifications in

just 30 days, rather than months. Prototypes arrived in two months, not four. The result: The new drives will be ready just 15 months after conception.

Still, Berkley concedes that he needs to do better. Despite the new teams, Quantum's 2½-inch drives are three months behind the original plan, partly because MKE had trouble making a new component. That, says Conner Vice-Chairman William J. Schroeder, underscores the weakness of relying on MKE. Indeed, one major Quantum customer worries that if sales continue to slow, MKE may not invest in new diskmaking technology, perhaps leaving Quantum drives less competitive.

But Berkley isn't placing all his bets on his Japanese partner. Quantum has just opened a new plant in Milpitas with some of MKE's technology. Back in the 1970s, Berkley learned the hard way how quickly Japanese suppliers can become rivals. As an executive at printer maker Qume Corp., he "watched a business disappear in two or three years" to Japan. So far, he has managed a neat trick in disk drives: using Japanese knowhow to help keep the U.S. on top.

By Robert D. Hof in Milpitas, Calif.

A WILD CARD IN THE DATA STORAGE GAME

In the 18 years since IBM created the Winchester hard disk—a sealed disk drive that stores data on metal platters—engineers at companies such as Quantum Corp. have made astounding strides. The first drives stored 35 megabytes of data on 14-inch platters. Today, disk makers cram 85 megabytes on 2½-in. platters. By next year, 1.8-in. drives will be available.

But there are limits in creating the tiny motors, platters, and recording heads to build ever-smaller drives. So a new technology is emerging that goes where "rotating memory," such as hard disks, can't. It's called the memory card—a bunch of memory chips crammed into a plastic cartridge about the size of a credit card.

NEW SPIN. NEC Corp. was the first to use the technology. Now, Hewlett-Packard Co. and Poqet Computer Corp. have it in their tiny "palmtop" PCs. The cards are smaller and lighter than disk drives, and retrieve data faster. With no moving parts, they can survive harsh environments such as factories. And they use little power, so a palmtop can run off two AA batteries.

As the market for palmtops and other tiny PCs grows, so will sales of memory cards. One researcher, SRI International Inc. in Menlo Park, Calif., says the market could swell from 4 million units this year to 52 million in 1993. The business got a big boost last year when two major groups of computer and electronics makers agreed on a standard for card size and software. IBM, Compaq, and Fujitsu are among the dozens who back it.



AN HP PALMTOP: DATA WITHOUT A DISK

But disk-drive makers aren't about to lose sleep over memory cards. One reason is price. A 4-megabyte card now costs \$720, compared with as little as \$150 for a 40-megabyte hard disk drive. And in memory cards, 4 megabytes is maximum capacity now. But 16-megabyte cards are expected by 1993, and 40-megabyte cards are likely by 1996.

FLASH CARDS. That has chipmakers diving into the memory-card business. Intel Corp. is leading the way with cards that use so-called flash memory. Unlike other chips used in memory cards, flash chips don't need a battery to keep them from losing their memory. And flash promises to be cheaper: By 1996, claims Richard D. Pashley, general manager of Intel's Memory Components Div., a 40-megabyte flash card will cost about the same as a 40-megabyte disk. Intel's Japanese rivals, including Fujitsu, Mitsubishi Electric, NEC, and Toshiba, are ramping up production of flash memories.

Still, hard disks aren't about to disappear, particularly when buyers of desktop PCs are asking for greater disk capacities. But in portables—where space comes at a premium—and in rugged systems, memory cards may knock disk drives out. Unless, of course, those disk engineers perfect the half-inch Winchester.

By Sunita Wadekar Bhargava in New York, with bureau reports

CHRISTIAN PUBLISHERS COUNT THEIR BLESSINGS

Updated themes and 'crossover' hits have sent book sales soaring

Three years ago, Roger L. Riether, a burned-out minister looking for a new career, and his father-in-law, Jerry E. Anderson, an insurance agent with a zeal for the gospel, bought a religious bookstore in a onetime parish in Greeley, Colo. They quickly discovered that old-fashioned Christian bookselling was a money-losing venture. Then a year ago, the two shut the store and resurrected it as Hidden Manna, a hip Christian boutique in Greeley's new mall. It's a hit. The shop stocks everything from nativity globes to cassettes by heavy-metal band Barbed Cross and T-shirts of a Jesus shouldering a cross with "Bench Press This!" emblazoned on it. But the big draw still is books. "I want to see something that tells people about the kingdom," says housewife Billie Lou Gaiser, who bought a gift.

Christian books a hot market? Well, if you think religious publishing still just means Bibles and treacly Sunday-school texts, guess again. Some 100 Christian publishers issued 4,500 new titles last year, up 33% in five years. And the nation's 5,000 Christian bookstores had sales of \$2.7 billion, up from \$1 billion in 1990. "The ministry is reaching people with the message of Jesus Christ," says Riether. "Our method is retailing."

TOUCHY-FEELY. The books sell well largely because they now tackle once-taboo subjects such as divorce, homosexuality, incest, AIDS, and wife abuse. Evangelical books these days are frank. Zondervan Publishing House's *Turn of Mind: Fear to Hope*, a man even calls his wife a "whore" and a "bitch." And they offer practical advice rather than just angel prayer. Women are told to leave their husbands if they feel they're in danger, for instance.

There's plenty of fiction, too, following the success of Janette Oke, the Laurinda Wilder of the Bible set. Oke's best novels of pioneer life, published in Minneapolis' Bethany House Publish-



ers, have sold 8 million copies since 1979. They're now issued in runs of 250,000, vs. 5,000 to 25,000 for most novels.

All this activity hasn't escaped mainstream publishers. Secular houses have long printed scholarly religious books, of course. But evangelical books are touchy-feely: They tell you that Jesus loves you, not that God is dead. To get such books on its list, HarperCollins Publishers Inc. paid \$60 million in 1988 for Zondervan in Grand Rapids, a major evangelical imprint. Now, Zondervan and HarperCollins' trade division cooperate to tap each others' markets.

The religious publishers, meanwhile, are broadening their audience with

"crossover" books. An example is *Why America Doesn't Work*, from Word Publishing in Irving, Tex. A treatment of the work ethic by Charles W. Colson, of Watergate-scandal fame, and Jack Eckerd, the drugstore magnate, it is expected to sell more to the trade than to Christian bookstores. Another sign of crossover: In February, *Publishers Weekly* began a best-sellers list for religious books sold in trade bookstores.

SUPERMARKET EVANGELISM. Baby boomers, who now fill many evangelical church pews, are a major reason for this transformation. They demand sophisticated self-help guides and books that explain events beyond their control.

For instance, Zondervan's *Armageddon, Oil and the Middle East Crisis*, which applies Old Testament prophecy to the Middle East, has sold a million copies since January. *The Thoughtful Christian's Guide to Investing* is doing well, too.

Publishers now are working on reaching the 75% of the U.S.'s 40 to 50 million evangelicals who never go into religious bookstores. Zondervan uses direct mail and is testing spinner racks in California supermarkets. And Word just sold Wal-Mart Stores Inc. a record 125,000 copies of *A Mother's Manual for Summer Survival*, a guide to keeping kids busy. "More Christians go into Wal-Mart on a weekly basis than into Christian bookstores," says Word Executive Vice-President Byron D. Williamson. He's also teaming with Sony Corp. on wholesome videos for kids.

Despite their new savvy, most Christian publishers still approach their business with missionary zeal. Word Publishing plays hymns and prayers for telephone callers on hold. And evangelical publishers try to sign only those with conservative religious convictions. The Christian Booksellers Assn. journal even ran an article on how to check out authors by talking with pastors and relatives and verifying college records.

The publishers may have to move more into the mainstream, however, if they want to keep increasing sales to self-indulgent baby boomers. Devotionals and missionary biographies gather dust on the shelves. So do books encouraging self-sacrifice. Baby boomers may have found religion, but they're not about to don sackcloth and ashes.

By Sandra D. Atchison in Greeley, Colo.

TISCH THE YOUNGER TAKES HIS TURN

Bob's new tasks: Keeping the football Giants in glory and helping to rescue New York City

There are few things Bob Tisch loves more than working a crowd. So the gregarious co-chief executive of Loews Corp. was beaming as he marched into Washington's Convention Center on June 13. The event was a black-tie fund-raiser for President Bush, a gathering of more than 4,000 movers and shakers. Never mind that Tisch is a Democrat; he knows everyone. But after scanning the room for a familiar face, his grin suddenly turned to chagrin. "I've never seen these people before," he groaned. "They're all new." A few moments later, as Tisch walked by a small knot of guests, a fellow party-goer called out: "Hiya Larry!"

Preston Robert Tisch, 65, has always been the "other" Tisch, friendly second fiddle to his steely brother Laurence. Although they built Loews into a \$12.6 billion-a-year conglomerate together, Larry's financial wizardry has long overshadowed Bob's achievements in operations. While Larry became a household name when he took over as chief executive of CBS Inc. in 1986, Bob's closest brush with fame was an undistinguished stint as Postmaster General. **MAJOR CRISIS.** But now, at an age when many executives think about retiring to the links, Bob Tisch has begun stepping out of his older brother's shadow. This spring, he paid more than \$75 million for 50% of the New York Giants pro football team. Not long before, New York Mayor David N. Dinkins appointed him the city's Ambassador to Washington, a fluffy-sounding job that actually carries some heavy responsibility. With his hometown in a major fiscal crisis, Tisch is lobbying hard to increase federal aid for New York. As chairman of the New York City Chamber of Commerce, a job he took last summer, he is also busy trying to stem the tide of companies exiting the city.

Tisch's new activities have led New York gossip to suggest that the two brothers have had a split. But they both deny it. "There's never been a conflict between Bob and myself," says Larry,

68. "But that doesn't mean we have the same enthusiasm for everything we do."

A lifelong football fan, Tisch has been trying to buy a team for years. He looked at the New England Patriots in 1988 but balked at the estimated \$80 million asking price. More recently, he tried to land a franchise in Baltimore. "It was an emotional buy," he says of the Giants, adding: "I wanted something for my kids to enjoy." How much he will enjoy it remains to be seen. In mid-July, the Giants start defending their Super Bowl championship with 13 unsigned

On Wednesday, Tisch heads to Giant Stadium for a caucus with co-owner Wellington Mara. He and Mara mainly use this weekly meeting to sign checks and discuss ways to boost the club's income. Although the Giants make their home in the nation's largest market, they are "about in the middle" of the league in terms of profitability, Tisch says. The Giants have already found one way to raise their income: They recently decreed that season-ticket holders must buy \$52 worth of pre-season tickets as well. Tisch and Mara are holding off on other options until next year.

POPPING CASHEWS. Once he and Mara are finished, Tisch hops back into a chauffeured car for a ride over to Teterboro Airport, where his Canadair Challenger 601 is waiting. Tisch paces about the cabin in his stocking feet, popping unsalted cashews against his diet doctor's advice. "I lost 24 pounds but gained 10 back," he says, explaining why he hasn't returned the doctor's recent calls.

Tisch is on his way to Washington to put in some good words for New York. With AIDS, homelessness, crack, and a \$3.5 billion budget gap, it's even worse off than during the 1970s' fiscal crisis. He knows there's only so much he can do—and even that probably won't be enough. "The whole Northeast is in bad shape," he says. "But New York..." He finishes by shaking his head.

Tisch takes his nonpaying "ambassadorship" seriously. Thursday morning, after breakfast at the Loews L'Enfant Plaza, he stops by the New York lobbyist's office for a 45-minute chat with Director Judy Chesser. They discuss funds to repair New York City's bridges as well as money for AIDS services. Next he's off to see House Speaker Thomas S. Foley. With a transportation bill pending, Tisch reminds him that New York desperately needs bridge-repair money. "Bob is a soft sell," says Foley aide Thomas R. Nides. "He won't come in with a laundry list. He can get the message across without it."

BOB TISCH: FROM HOTELS TO HUDDLES

BORN Apr. 29, 1926, Brooklyn

EDUCATION B.A., University of Michigan

FAMILY Wife Joan; three children

POSITION President and co-chief executive of Loews Corp., which includes hotels, CNA Insurance, and Lorillard cigarettes. His 14% share is worth \$966 million

OWNER 50% share of New York Giants football team, worth an estimated \$75 million

CURRENT OUTSIDE ACTIVITIES INCLUDE:

Chairman, New York City Partnership
Chairman, New York Chamber of Commerce
New York City's Ambassador to Washington

veterans, a quarterback quandary, and a rookie head coach. But Tisch is optimistic. "We'll have a very good team, good enough to make the playoffs," he promises.

Like Larry, who has his hands full with CBS, Bob Tisch is taking a less active role at Loews these days. Responsibility for daily operations belongs mainly to Larry's sons James and Andrew, as well as Bob's son Jonathan. But Tisch's schedule isn't getting any lighter.

A typical week in June begins with him attending the Persian Gulf war parade with Mayor Dinkins, sitting down for a big Convention & Visitors Bureau luncheon, and joining scores of screaming kids at a children's museum party.



A lifelong fan, Bob
shopped for a football
team for years before
paying \$75 million
for 50% of the Giants

later, Tisch dances a couple of late-night routines. Leaving the Republican Center, he meets Tim and Nancy in the elevator. Since Tim is wearing a tux, Tisch guesses they're going to some party and offers a lift. The boys' eyes widen when they see a stretch limo waiting outside. "Use me, you," asks Tim, a Cornell classmate. "My company runs the town," Tisch explains nonchalantly as they get into the limo. "Tell me what you do."

HELPING FATHER. After dinner, Tisch jets into Teeter, no arriving at 11 p.m. There is no rest for the partygoers. The next day, he's up to give an 8 a.m. breakfast speech for the New York City Chamber of Commerce. Exhausted, he calls it a day at 8 p.m. Tisch and his wife of 40 years head for their

home in Manhattan.

It's a long way from Teeter, the nation's classiest set of hotels, to the Pines. Spruced up, the hotel became a success, and the Tisch brothers were in business. They kept no other hotels in Atlantic City and Miami before turning to New York City in 1960.

Since then, they have added tobacco, insurance, watches, oil rigs and tankers, and a lot more. While Larry concentrates on buying assets, Bob oversees them and makes sure they run smoothly. The one exception is CBS, where Larry

has taken the reins from the start.

Until now, Bob Tisch's lone experience in Washington was two years as first assistant defense attorney. The job was difficult, Tisch says, but he learned a lot and had fun. "I was a lawyer without having to arbitrate. Critics contend he caved in too easily to labor demands instead of seeking needed concessions. I think the union was crying tears when he left," says Gene A. Del Polito, executive director of the Third Class Mail Association.

Now, on the eve of his first football season as an owner, Tisch is hoping to keep Giants fans happy. First task: winning the preseason opener against the Buffalo Bills, the team they defeated last January in the Super Bowl. Unfortunately, as Tisch well knows, that will be a whole lot easier than putting New York City back on its feet.

By Bruce Hoptman and John

ADVICE FOR WOULD-BE ADVISERS

A year ago, Errol Alexander got laid off from his job as head of market research at Amex Life Assurance in San Rafael, Calif. Despite degrees from West Point and Harvard business school and a solid working background, the 50-year-old Alexander found employment pickings quite slim. So he chose a path well trodden these days by execs from the corporate world: He became an independent management consultant. Now, after what he admits has been a tough year, his one-man firm, Alexander & Associates, "is on the verge of turning the corner" to profitability.

Like other newcomers to the growing ranks of consultants, Alexander is betting there's an upside to the business downturn. He is counting on companies to use consultants on projects that would normally have been handled by in-house staff. But such people have often been dropped from the payroll. "The combination of downsizing and corporate budget-watching is producing what I think will be the trend for the '90s—contract employment," says Kent Black, group vice-president at Drake Beam Morin, a leading outplacement firm.

DROPOUTS GALORE. The field is becoming increasingly crowded. By one estimate, 450,000 Americans call themselves independent consultants. Still, if you believe that your job is endangered or if you feel constricted in the corporate milieu, joining the ranks may be a gamble worth taking. Successful consultants

often charge lawyer-like fees of \$150 to \$400 an hour or \$1,000 to \$2,000 a day—though you'll probably have to start out charging considerably less.

Don't assume that just hanging out a consultant's shingle is a ticket to success. Three out of four newcomers to the field give up after one year, and 90% seek a regular job after two, according to industry newsletter *Consultants News*. Why the high dropout rate? "In every recess-

Says Alexander: "The least credible approach to a client is to say: 'I can do anything. What do you need?'"

FEET OF CLAY. If the evaluation is honest, it will pinpoint weaknesses. "Not every corporate exec is likely to be good at everything that a consultant should be good at," explains Ted Moline, who formed Janus Consulting in Reston, Va., last year, after Saatchi & Saatchi sold a consulting subsidiary where he worked. "If you're good at taxes, you might not be good at dealing with clients. If you have technical skills, you might not have a solid understanding of how business works."

When he's not working on staff-training projects for outplacement firms, Moline hands out advice in a seminar series, *Fundamentals of Management Consulting*. Offered by the Council of Consulting Organizations (CCO) in New York and taught by pros in various cities (box), the seminars point out some of the many things fledgling consultants have to learn before they can even think about business cards.

One avid student was Joan Beavin, a former vice-president at Amex Life Assurance who had brought Alexander into the company. Increasingly unhappy with the corporate culture, she resigned last year to head Beavin & Murphy Associates, a two-person consulting firm in Mill Valley, Calif. One skill she found she lacked: sales. "I never had to sell myself before," says Beavin, who took the *Fundamentals* course to

FIRST, MAYBE YOU SHOULD CONSULT...

BOOKS

- ▶ *Management Consulting: A Guide to the Profession*, by Milan Kubr (International Labor Office, \$39)
- ▶ *The Consultant's Calling*, by Geoffrey Bellman (Jossey-Bass, \$25)

MONTHLY NEWSLETTER

- ▶ *Consultants News*, \$144 a year, from Kennedy Publications, Templeton Rd., Fitzwilliam, N. H. 03447; 603 585-6544

THREE-DAY SEMINAR

- ▶ *Fundamentals of Management Consulting*, \$590; New York, Aug. 5-7; Denver, Oct. 7-9; Las Colinas, Tex., Nov. 8-10; for other cities, call 212 455-8220

DATA, BW

sion, lots of people who get laid off think all you need to become a consultant is \$15 for business cards and an office in the basement," says the newsletter's publisher, James Kennedy.

A first step in beating the odds is making a realistic self-evaluation that lets you identify a niche where you can apply your skills: market research, economics, personnel training, or whatever.

learn to write proposals and make presentations.

Before you spend time and money to outfit an office and develop new abilities, make sure you're really consultant material, advises Scott Halliday, CCO's director of member services. "Can you cope with the big cultural and environmental change, working without all the things you took for granted at the corporation?" he asks. "There's no support staff. No benefits. No office camaraderie to help relieve the pressure." Attempting to sell your services over and over means a lot of rejection. Halliday asks: "Are you thick-skinned enough to keep from getting discouraged?" Adds Sharon Epstein, who joined the Agency for International Development in Washington after leaving the U.N. Population Fund to take a fling at consulting: "The hardest thing about being a consultant was returning every few weeks from an overseas project and having to say: 'Well, I'm back again. Do you have any work?'"

If you have doubts about



ing yourself, the pros have suggestion. Rather than go in your own, offer your expertise to an established consulting firm. Often, this can be done on a split-fee, part-time arrangement, where the firm calls on your talents as needed for specific projects. Once you've proved yourself to the client, you may get hired in directly next time," says Kennedy.

WISDOM MATES. Or hook up with a partner whose strengths complement your own. Working with professional service firms in the \$1 million to \$5 million range, Beavin, for example, consults on operations and organizational development, while her partner, Kim Murphy, handles marketing and planning assignments. "In the first year, not having someone to talk to was a big boost," says Beavin. To minimize taxes and avoid personal liability, you'll want to ask a lawyer how best to structure your business: sole proprietorship, S-corporation, or partnership. If an assignment requires you to rely on input from another con-

sultant (one who specializes in, say, employee compensation or public relations), it's a good idea to have the lawyer draw up a contract for the client to sign. It should make sure you won't owe the subconsultant money. But the pros add that the majority of projects are undertaken with a handshake or verbal agreement on the phone.

"Even the biggest companies usually say: 'Just send your invoice for so many hours,'" says David Horwitz, a former producer on the *CBS Evening News*, who left eight years ago to form Media-

Prompt, in Stamford, Conn. The consulting firm has trained execs of Perrier, Union Carbide, and a General Motors division for media appearances and crisis management. Some projects, Horwitz says, are so loosely stated that a lawyer would find it hard to detail in a contract exactly what might or might not be done.

Once you decide to take the step, don't make a halfhearted commitment. It's too often true, complains Kennedy, that a consultant is "someone who's really looking for a job." Alexander acknowledges

that his firm got off to a slow start because he hedged his bets, "trying to do a job search and line up clients at the same time."

Eventually, Alexander landed a contractual assignment from his former employer. The task: to brief department heads and staffers on the value of the market profiles he had done before he received his pink slip. "Funny, but when you're at a company, your work can be underappreciated," he muses. "Then, you come in from outside and show someone what an incredible resource the work represents, and you get an enthusiastic reception."

'ON TRACK.' The chance of doing consulting work for a former employer is a good reason not to burn any bridges. Another consideration: Have a startup business plan that looks ahead at least a year. Beavin and Murphy budgeted living expenses against projected income for two years, "but saw we were on track after nine months," Beavin says. "So we hung in and even made some money by the end of the year." Noting that in the early months, he had "maxed out my credit cards" and confronted a heavy negative cash flow, Alexander says he took the "& Associates" route to help land assignments. He agreed to lend his expertise to a half-dozen other consultants who specialize in different areas.

For the man or woman who works alone, a major concern is finding time to prospect for new clients while busy on assignments. "We try to devote at least 10% of our time to networking and making personal sales calls," says Beavin. When a project ends, some consultants find it difficult to shift gears and don a salesperson's hat. After all, a major attraction of the consultant's life is the freedom to set your own schedule. To complete an assignment on deadline, you might choose to work 14 hours a day. But once you complete a job, it takes willpower to resist the temptation to head for the beach.

Don Dunn

THE REALITIES OF CONSULTING

- 1 The employer who fires you is often the best prospect to become your first client—if you didn't burn any bridges behind you
- 2 There's no formula to help you decide how much to charge. Established firms staffed with consultants who earn \$35,000 a year typically charge \$80 an hour; ones where employees earn \$60,000 charge \$125
- 3 Your independence doesn't mean you call the shots. Winning and keeping clients can require more hand-holding and politicking than it takes to climb a corporate ladder

Health

A VASECTOMY WITHOUT THE UNKIND CUT

Each year, about 400,000 men in the U. S. have vasectomies. Usually done on an outpatient basis, the procedure typically takes less than 20 minutes and entails little medical risk. But now, U. S. doctors are using a new technique that makes the operation even quicker and safer. Called a no-scalpel vasectomy, it eliminates a major fear many men must conquer before they can consider this family-planning option.

The no-scalpel method was developed in China and has already been performed on some 8 million men. In the late 1980s, a medical team led by Marc Goldstein of New York Hospital-Cornell Medical Center studied the technique in China and returned to teach it to American physicians. Now, says the Associa-

tion for Voluntary Surgical Contraception in New York, about 300 urologists and family-practice doctors are trained. "Every doctor who learns it switches," says Sheldon Freedman, a Las Vegas urologist who routinely performs five no-scalpel vasectomies a week.

NO NICKS. In the traditional method, doctors numb the scrotum with a local anesthetic. Then they use a scalpel to make one or two 1/4-inch incisions to reach each of two thin tubes, called vas, through which sperm travel to the seminal fluid. The new technique dispenses with the scalpel, reducing the risk that a blood vessel might be nicked accidentally. Instead, the doctor uses a specially modified surgical clamp with sharpened points. One point makes a single puncture (so small it's invisible to the patient) through which the doctor reaches to snip each vas.



It takes about 10 minutes to cut and tie the vas ends with thread or tiny clips—40% faster than a traditional vasectomy. No stitches are needed, and the AVSC says minor complications occur in only 4 out of 1,000 cases, vs. 31 per 1,000 with the standard method.

Typically, the procedure costs \$250 to \$750. As is the case with female tubal ligation (commonly known as "having the tubes tied"), a microsurgeon may be able to reverse a vasectomy—but that requires a hospital stay and \$5,000 or more. Although the no-scalpel procedure is less injurious than the older method, the odds on reversal are low. "So much depends on how the vas ends are closed and the health of the sperm," says Dr. Larry Davis of the University of Tennessee Medical Center.

Poor odds or not, reversals do occur, notes Thomas Berglund, a family practitioner in Portage, Mich. Among his 500 patients who underwent a no-scalpel vasectomy in the past year was one who'd had an earlier vasectomy reversed—and fathered a child with his new wife. "He said the second procedure was a breeze," Berglund says. *Don Dunn*

With state income taxes on an upward march, tax-exempt municipal bonds have an almost irresistible appeal. But while munis are free from federal, and in many cases, state taxation, the muni market is rife with credit concerns and downgraded bond issues.

Muni bonds, the debt obligations of state and local governments, have long been considered safe investments, but "it's hard to make blanket statements about them anymore," says Nancy Utterback, a vice-president for municipal research with Kidder Peabody. As the fiscal crises of many states and cities escalate, downgraded munis outnumber upgrades by 3 to 1.

Essential-service revenue bonds, such as water, sewer, and electricity bonds, are stable bets. "In many cases, they're the least affected by local economic disturbances,"

AVOIDING POTHoles ON THE MUNI ROUTE

says George Friedlander, managing director of fixed-income strategy for Smith Barney, Harris Upham. He likes the long-term bonds of the New York State Power Authority and the Los Angeles Dept. of Water & Power. They yield about 7.1%.

Utterback prefers the revenue bonds of Florida's Jacksonville Electric Authority and Utah's Intermountain Power Agency. The Jacksonville bonds maturing in 2012 yield about 7%; 30-year Intermountain Power Agency bonds yield about 7.25%. Because they're free from federal taxation, an equivalent taxable yield would top 10%.

Buying insured muni

bonds is a good safeguard. If an issuer defaults, the bond insurer makes interest and principal payments. There has been some concern about whether the insurers have

The safest munis: Treasury-backed 'pre-refunded' bonds

the assets to cover a raft of defaults, so check that the insurer is rated AAA by Moody's and S&P. "Unless problems get a lot worse, I'm still comfortable with the insurers," says Friedlander.

Smart Money

"They have to meet a 'stress test' to get an AAA rating." If you want "both belt and suspenders," he suggests, buy insured essential-service bonds, which yield about 7.1%. Similar uninsured bonds yield about 7.2%.

SHORT AND SWEET. The ultimate safe munis are "pre-refunded" bonds. Pre-res are backed by an escrow account of U. S. Treasury securities. Cash flow from the Treasuries pays off the bond interest and principal. Since many pre-res reach maturity in the next four years, they are a short-term investment. You can find a four-year pre-refunded yielding about 5.75%, equal to an 8.33% taxable yield for someone in the 31% bracket.

If you want to spread your risk, there's no shortage of muni-bond funds. There are 486 muni-bond funds to choose from, 295 of which specialize in single-state issues.

Suzanne Woolley

**ONE OF THE BIGGEST THINGS WE EVER ACCOMPLISHED
WAS BECOMING THIS SMALL.**



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The Energy To Change



Travel

GO TAKE A HIKE—AND A MASSAGE, AND YOGA, AND . . .

When my co-workers heard I would be visiting two spas in the Southwest, all I got were jokes about mud baths and pedicures. Instead, I found myself struggling through 6 a.m. yoga classes that were warm-ups for brisk, steep mountain hikes.

The '90s version of the spa vacation—more like a fitness holiday than the fat-farm pampering of yore—isn't for the fainthearted. Sure, you can loll around the pool waiting for a massage. But if that's all you want, why pay Rancho La Puerta \$1,200 to \$1,900 a week or Canyon Ranch \$2,210 to \$2,590?

Truth be told, invigorating yoga stretches in front of a crackling fire are a nice way to start the day at Rancho La Puerta (800 443-7565). Then, it's up Mount Kuchumaa with a band of friendly hikers to enjoy the fresh desert air and the wide vista of rocky slopes.

HAPPY CAMPERS. Breakfast in the Rancho's Spanish-style dining hall is a smorgasbord of cereals, fresh-baked bread, fruit, and granola. The first of the day's five exercise classes begins soon after, choose anything from aerobics and weight lifting to tennis and swimming.

Everyone arrives on Saturday at the Rancho, on the outskirts of Tecate, Mexico, about an hour southeast of San Diego. Some 150 guests go through group orientation, sign up for classes in healthful cooking, Indian lore, or self-defense, and dine together at large tables. The atmosphere is friendly and camp-



like; many people come back the same week every year.

Although the Rancho's older rooms are spartan, its new villas boast wood-beamed ceilings and Mexican-tiled baths. The far-flung villas give visitors a sense of privacy amid stunning landscaping.

Rancho La Puerta stresses a spiritual approach to fitness

that emphasizes the mind's role in maintaining a healthy body. Well-taught sessions in yoga, t'ai chi ch'uan, and meditation are part of the spa's "fitness buffet."

Canyon Ranch in Tucson, Ariz. (and in the Northeast in Lenox, Mass.), covers a lot more ground than Rancho La Puerta. The resort (800 742-9000) offers a huge assortment of classes dealing with executive stress, sleep disorders, crafts, and astrology—though often at stiff additional fees. It also has programs for quitting smoking or losing weight, and it's involved in

the weather conditions and fitness level of the hikers.

The ranch also provides mountain bikes and guides for strenuous but scenic rides through nearby Sabino Canyon. Tennis, squash, and racquetball are available, too, along with dozens of exercise classes.

SYBARITIC MENU. Of course, after a day of intense exercise, even my puritan conscience is convinced that I'm entitled to a bit of pampering. Canyon Ranch offers a great choice of sybaritic pleasures: massages, facials, mud baths, and wraps.



Mud baths and mountain biking at Canyon Ranch: A full fitness menu, plus programs to quit smoking and help sleep disorders

longevity research. Like Rancho La Puerta, Canyon Ranch wants visitors to adopt healthier habits of eating, exercising, and relaxing.

Canyon Ranch offers its 285 guests lots of one-on-one guidance: consultations with a nurse and program coordinator, and 15-minute private consultations including body-fat analysis and nutrition and exercise advice. The rooms, in small, one-story buildings, are hotel-like.

No, they don't starve you here. The food is light and low fat and includes salad and pasta bars. One woman's Tucson relatives offered to meet her at Canyon Ranch's front gate with a pitcher of margaritas if she got desperate. No booze is served at the ranch, but the woman relaxed after she got a second dessert on her first night.

One of Canyon Ranch's biggest draws is hiking. Each morning, the ranch shuttles guests to trails chosen to suit

As an aromatherapist rubs me with scented oil in a dimly lit room where New Age music plays softly, I sink into a supple stupor. This is, after all, what the spa experience is all about. *Kathleen Kerwin*

Worth Noting

■ **TUITION TAB.** A private college education for a child now 10 will cost more than \$114,000, estimates Neuberger & Berman Management. The investment firm offers a free pamphlet that includes saving strategies and a tuition-planning worksheet. Call 800 877-9700.

■ **HOMEWORK.** More than a mortgage calculator, *Buying Your Home* software for a PC lets you plug in family financial data to see what you can afford, whether it's best to buy or rent, and how ownership will affect taxes. At computer stores, from Home Equity Software, it's \$59.



Lush landscapes and well-taught yoga at Rancho La Puerta stresses the mind's role in maintaining a healthy body

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Original concept courtesy of Lewis & Partners, San Francisco

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make a living. But thanks to ACCION, people who only one year ago were barely able to keep their families alive, today have paid their loans back in full and have been given a chance to better their lives.

More importantly, they've been given back their dignity. All it takes is for you to believe in them.

For more information or to send a contribution, write to ACCION International, 1385 Cambridge St., Cambridge, MA 02139 **617-492-4930**.

ACCION International

Index gives the starting page for a story or feature with a significant reference to a company. Most directories are indexed under their own names. Companies listed only in tables are not included.

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For those willing to do the proper research, history has always proven to be a valuable ally.

With great clarity and absolute objectivity, it tells you which companies have performed the most reliably, and managed their investments with an eye toward economic change. And, in the case of Mutual Of New York, it reveals a legacy of success that



no other insurance company has been able to duplicate.

Each and every year, for the past 148 years, Mutual Of New York has consistently returned a dividend to its policyholders. Through peacetime and through war. Through depression and expansion alike, our policyholders have always enjoyed a share in our gains.

YES, BUT WHAT HAVE WE DONE LATELY?

Over the course of the past year, Mutual Of New York has again managed to turn recession into expansion.

Our revenues have increased by 6% to \$4.6 billion, a rate of growth



The Wrights conquer the air above Kitty Hawk.

that outstrips most of the industry. Our assets under management grew 6% to \$23.1 billion.

Our life insurance in force grew 8.5% to \$67 billion. And, remarkably, 70% of our new sales came from existing clients, and from people they referred to

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PUT HISTORY ON YOUR SIDE.

Together, all of these facts and figures add up to a very good record. And a very good omen.

For, as you've undoubtedly heard, history tends to repeat itself. And, after 148 years of consecutive dividends, Mutual Of New York policyholders are looking forward to an encore.

If you'd like more information on Mutual Of New York's past, its present, and on how our plans can impact on your future, simply call 1-800-473-6669.



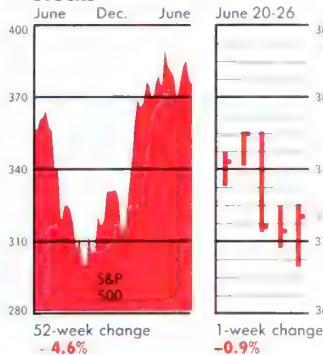
MUTUAL OF NEW YORK MONEY FOR LIFE

Investment Figures of the Week

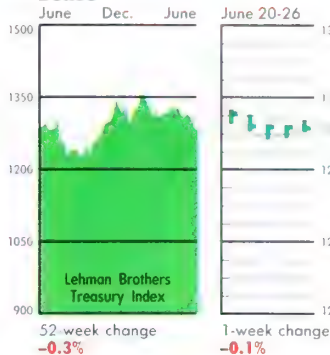
MARKET COMMENTARY

Pressures that the Big Four Japanese brokerages made up for customers' losses pummeled the already beaten-down Tokyo market, knocking 2.1% off the Nikkei on June 24 alone. Japanese stocks followed, with the Nikkei dropping 53 points, or 1.7%. A sell-off in technology stocks sent the Russell 2000 down 3.1% for the week. There's a bright spot. The put/call ratio shot up to 0.58. That's bearishness among speculators—and that's a bullish sign.

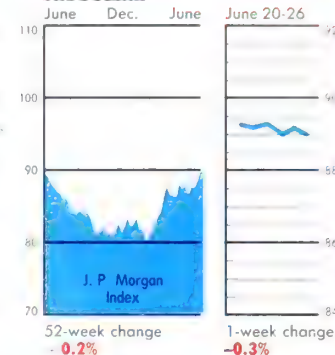
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS

	Latest	% change Week	% change 52-week
JONES INDUSTRIALS	2913.0	-1.4	1.8
COMPANIES (Russell 1000)	193.7	-1.2	4.8
ALL COMPANIES (Russell 2000)	167.6	-3.1	0.2
COMPANIES (Russell 3000)	205.8	-1.3	4.5

FOREIGN STOCKS

	Latest	% change Week	% change 52-week
FTSE 100 (FINANCIAL TIMES 100)	2443.2	-1.7	2.9
NIKKEI INDEX	23,766.4	-1.0	-26.4
TSE COMPOSITE	3481.1	-1.4	-1.1

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.7%	5.7%	8.1%
30-YEAR TREASURY BOND YIELD	8.5%	8.5%	8.5%
S&P 500 DIVIDEND YIELD	3.3%	3.2%	3.2%
S&P 500 PRICE/EARNINGS RATIO	17.7	17.8	16.3

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 26-week moving average	364.8	363.1	Positive
Stocks above 26-week moving average	59.5%	68.6%	Neutral
Speculative sentiment: Put/call ratio	0.58	0.49	Positive
Insider sentiment: Vickers sell/buy ratio	2.33	1.95	Neutral

INDUSTRY GROUPS

4-WEEK LEADERS

	% change 4-week	% change 52-week
INTERMARKET AUTO PARTS	13.6	8.5
PAPER CONTAINERS	11.6	20.8
MINING	10.0	-11.6
HAIRWARE AND TOOLS	9.4	-1.8
PHARMACEUTICALS	8.2	13.5

4-WEEK LAGGARDS

	% change 4-week	% change 52-week
HEALTH CARE SERVICES	-12.7	48.2
NATURAL GAS DISTRIBUTION	-11.4	-20.7
SEMICONDUCTORS	-9.8	-14.2
PUBLISHING	-8.3	-3.6
BROADCASTING	-6.8	-18.0

Strongest stock in group

	% change 4-week	% change 52-week	Price
GOODYEAR TIRE & RUBBER	35.4	5.9	33 1/2
STONE CONTAINER	19.3	24.5	21 1/8
NEWMONT MINING	13.1	-10.4	37 3/4
BLACK & DECKER	23.2	-3.2	15 1/4
CYPRUS MINERALS	27.1	4.6	22 7/8

Weakest stock in group

	% change 4-week	% change 52-week	Price
MANOR CARE	-18.5	28.3	18 1/8
COLUMBIA GAS SYSTEM	-55.1	-58.5	18 1/8
NATIONAL SEMICONDUCTOR	-21.4	-20.0	5 1/2
TIME WARNER	-22.9	-12.1	89 1/8
TELE-COMMUNICATIONS	-17.3	-10.3	13 1/8

BRIDGE INFORMATION SYSTEMS INC.

MUTUAL FUNDS

LEADERS

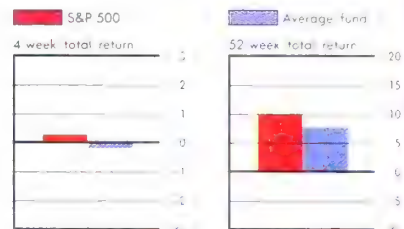
	% 4-week total return
STRATEGIC INVESTMENTS	19.9
STRATEGIC SILVER	16.2
FINANCIAL STRATEGIC GOLD	11.0

	% 52-week total return
DELITY SELECT BIOTECHNOLOGY	59.8
DELITY SELECT HEALTH CARE	51.9
DELITY SELECT MEDICAL DELIVERY	51.1

LAGGARDS

	% 4-week total return
EQUITY STRATEGIES	-8.9
DFA UNITED KINGDOM SMALL COMPANY	-7.9
FIDELITY EUROPE	-6.5

	% 52-week total return
BULL & BEAR SPECIAL EQUITIES	-42.1
STEADMAN OCEANOGRAPHIC TECHNOLOGY	-37.7
STEADMAN AMERICAN INDUSTRY	-30.8



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\$10,826

+0.11%



U. S. stocks

\$10,628

-2.10%



Money market fund

\$10,615

+0.11%



Gold

\$10,436

-1.78%



Foreign stocks

\$9,324

-0.68%

DATA RESOURCES INC.

Data on this page are as of market close Wednesday, June 26, 1991, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of market close.

June 25. Mutual fund returns are as of June 21. Relative portfolios are valued as of June 25. A more detailed explanation of this page is available on request.

EQUAL OPPORTUNITY: DON'T STOP NOW

In 1965, black Americans were largely outside the mainstream of the U.S. economy. But an unprecedented effort by the federal government wrought a massive social change. Badgered and prodded by Washington, corporations changed their ways and began large-scale efforts to recruit blacks—as well as women, Hispanics, and other minorities.

Progress for blacks has not come without cost. The push for equal job opportunities contained within it a dilemma when applied under what came to be known as affirmative action: Preference for some creates discrimination against others. Many whites resent the preferential treatment they see being given blacks, a feeling that has intensified as the economy's growth has slowed and corporations have squeezed employment. And many blacks have had to endure the suspicions of co-workers that they advanced because of the color of their skin rather than their abilities.

Affirmative action has been a substantial accomplishment despite these problems (page 50). Black participation in the work force has surged over the past 25 years, especially in big companies, thrusting millions of black families into the middle class. But this very success has erected barriers on the road to full equality. For too many companies, affirmative action has become a routine bureaucratic function. Minority workers are ordered up by the numbers and treated as so many interchangeable parts. Yet, enlightened companies have proved that it is possible to meet numerical hiring goals while keeping the focus on the individual employee. They do not hire unqualified, or even marginally qualified,

workers just to make a target, and they see to it that minorities have a chance to thrive. This approach is harder and the initial costs are higher to do things this way, but such an approach ultimately is far more productive.

So we have come a long way. Now, a task for the '90s is to open up the ranks of management. Far too often, minority management trainees are shunted off into staff jobs—often human relations—that represent dead ends on the corporate ladder. The relatively brief time that has passed since blacks were excluded from all management jobs helps explain their nearly total absence at the top. But until black managers are given key line positions, they will never make it to the upper reaches of management.

What remains to be done? Both parties are attempting to milk the debate about a new civil rights bill for their own benefit, while the argument has bogged down in a morass of conflicting opinions about quotas. We find it impossible to tell whether the proposed bills would involve quotas or not.

But there is a larger point to be made from the unifying argument over new civil rights legislation. The nation must remain committed to affirmative action because, as the business community recognizes, the nature of the U.S. workforce is changing. Less than one third of the 10.7 million jobs created between 1985 and 1990 were filled by white males and the proportion will be even smaller in the '90s. In other words, growth is going to come from minorities and women. Corporate America has no alternative but to develop the talents of these new, dynamic forces.

THE TOKYO MARKET NEEDS A TOTAL OVERHAUL

Now and then, the Western world is swept by a flurry of wishful thinking that Japan is undergoing some sort of fundamental change. In its latest guise, this illusion centers on the securities business. The presidents of two major Japanese securities houses, Nomura and Nikko, have resigned under pressure from the Finance Ministry because they favored big clients and lent money to Japanese gangsters (page 26). Will the shock waves also include a turn toward a Western-style standard of openness and fairness for Japan's financial markets?

Yes, it seems probable that Japan's top bureaucrats indeed want a cleaner market where stock manipulation, real estate speculation, insider trading, and underworld ties are reduced. In that sense, the crackdown will benefit ordinary investors.

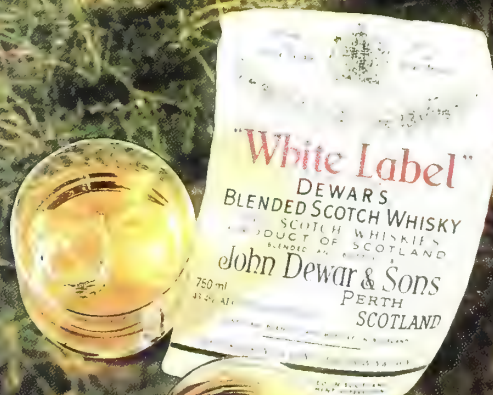
But it also seems fair to conclude that the reforms will be slow and grudging. Japanese securities firms have covered major clients' losses and consorted with gangsters for decades, with the full knowledge of regulators. The Finance Ministry has finally acted only after competition forced the

practice to self-destructive, publicly unacceptable proportions and the brokers kept pumping up the speculative and criminal elements that Finance now wants to crush.

Events that appear to be watersheds to outsiders rarely are so in Japan. When Takako Doi led the Socialists to unprecedented electoral victory two years ago, it supposedly augured a new political era in Japan. Doi recently resigned. The Socialists are in disarray, and the ruling party has high approval ratings. The aftermath of the 1989 Recruit scandal was to be cleaner Japanese politics. Little has changed.

Change in Japan sometimes seems agonizingly slow. But the government is now showing that when it is in the nation's interest to have a cleaner securities market, it can act with forceful speed. Wringing out the stock market cheats is part of the larger issue of overall Japanese financial market reform that includes liberalizing the yen, opening up banking markets, and fostering a more competitive securities industry. The challenge now is to persuade Tokyo's elite bureaucrats that the world's second largest capital market needs to be modernized in all aspects.

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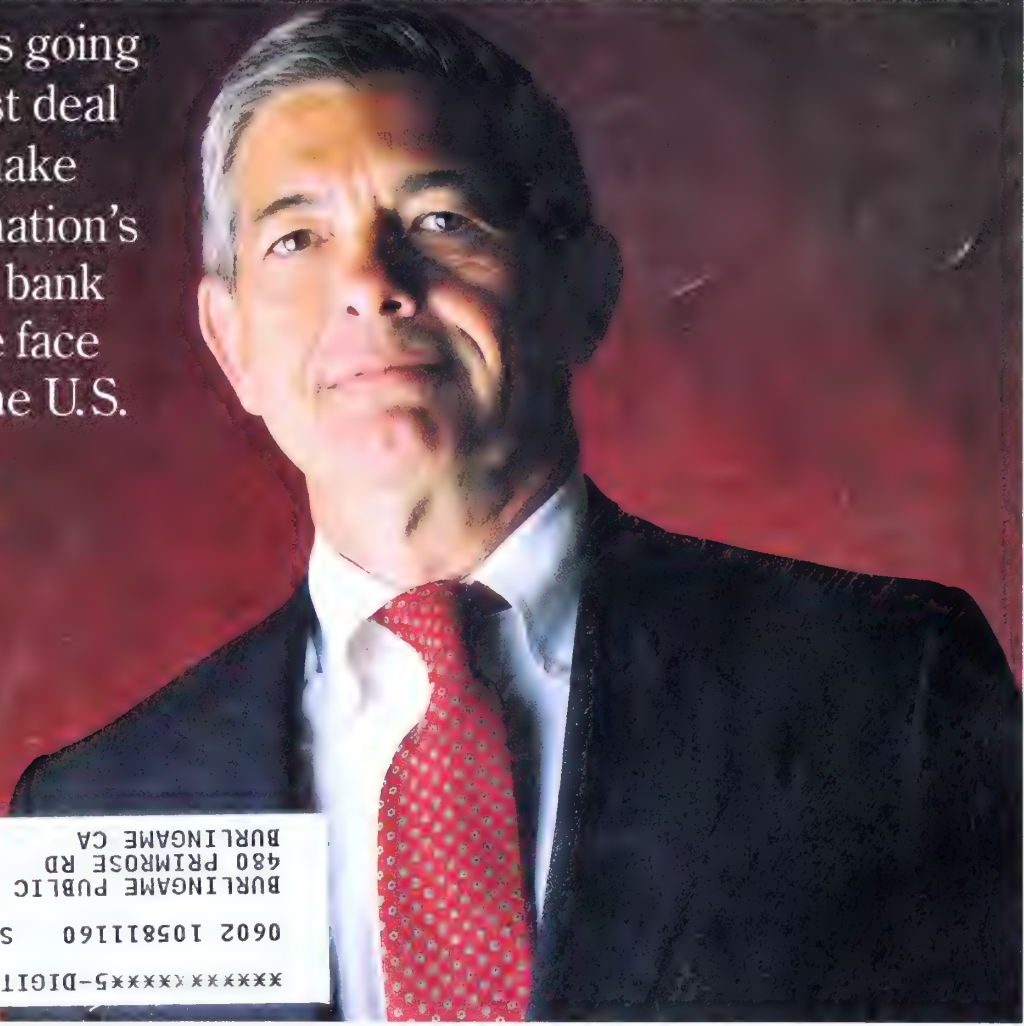
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SUPER BANKER

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Hugh McColl is going
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and change the face
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BRIDE AND GROOM? NCNB'S \$3.8 BILLION BID FOR C&S/SOVVRAN MAY SPUR MORE MEGADEALS AS 'SUPER-REGIONALS' TAKE CENTER STAGE

Cover Story

116 SUPER BANKER

If Hugh McColl can unite NCNB and C&S/Sovran, his 'NationsBank' will be the second-largest in the U. S. after Citicorp. The downside: McColl will have to overcome a culture clash and deal with C&S/Sovran's load of bad loans. The upside: Congress is likely to approve nationwide banking this year, making 'super-regionals' even tougher rivals to the big money-center banks

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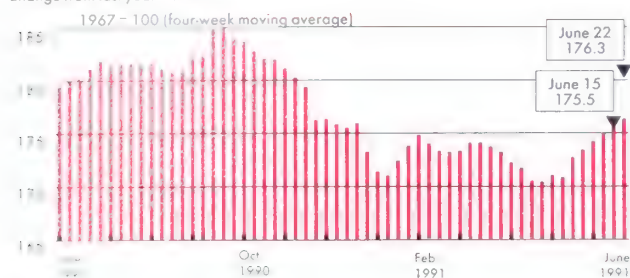
The real strengths of ESOPs

Business should rally round the labs

BusinessWeek Index

PRODUCTION

Change from last week: 0.5%
Change from last year: -2.7%

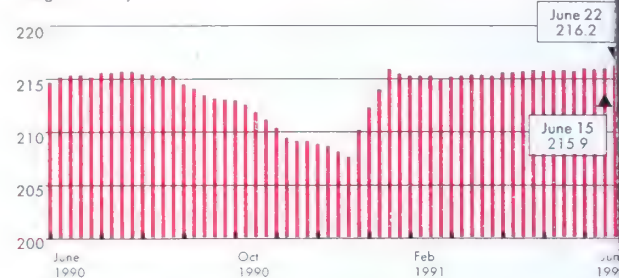


The **production index** was up sharply for the week ended June 22. On a seasonally adjusted basis, output of trucks and paper increased. Steel, auto, and paperboard production declined, while output of electric power, crude-oil refining, coal, lumber, and rail-freight traffic was flat from the previous week. As a result, before calculation of the four-week moving average the index was virtually unchanged at 177.8, from 177.6 in the prior week.

BW production index copyright 1991 by McGraw-Hill Inc.

LEADING

Change from last week: 0.1%
Change from last year: 0.4%



The **leading index** advanced slightly during the week ended June 22. A sharp drop in the number of business failures led the gain. Stock prices were higher, and the growth rates for materials prices and M2 both improved. On the negative side, higher bond yields and a lower growth rate for real estate loans. Before calculation of the four-week moving average, the index increased to 216.5, from 216 in the previous week.

Leading index copyright 1991 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (6/29) thous. of net tons	1,593	1,556#	-14.5
AUTOS (6/29) units	123,823	117,540r#	-13.8
TRUCKS (6/29) units	79,404	82,477r#	-13.9
ELECTRIC POWER (6/29) millions of kilowatt-hours	NA	62,839#	NA
CRUDE-OIL REFINING (6/29) thous. of bbl./day	13,906	14,011#	-0.5
COAL (6/22) thous. of net tons	19,481#	19,686	0.5
PAPERBOARD (6/22) thous. of tons	752.6#	762.3r	0.3
PAPER (6/22) thous. of tons	759.0#	739.0r	1.7
LUMBER (6/22) millions of ft.	548.1#	546.2	13.2
RAIL FREIGHT (6/22) billions of ton-miles	19.7#	19.6	-3.0

Sources: American Iron & Steel Inst., Ward's Automotive Reports, Edison Electric Inst., American Petroleum Inst., Energy Dept., American Paper Inst., WPPA, SFAA, Association of American Railroads

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (7/2)	139	138	151
GERMAN MARK (7/2)	1.83	1.78	1.65
BRITISH POUND (7/2)	1.60	1.64	1.79
FRENCH FRANC (7/2)	6.21	6.06	5.55
CANADIAN DOLLAR (7/2)	1.14	1.14	1.17
SWISS FRANC (7/2)	1.58	1.54	1.40
MEXICAN PESO (7/2) 3	3,008	3,007	2,863

Sources: Major New York banks. Quotations expressed in units per U.S. dollar, except for British pound expressed in dollars

PRICES

	Latest week	Week ago	% Change year ago
GOLD (7/2) \$/troy oz.	367.100	366.100	1.4
STEEL SCRAP (7/2) #1 heavy, \$/ton	89.00	89.00	-20.5
FOODSTUFFS (6/28) index, 1967=100	196.2	199.2	-14.0
COPPER (6/29) ¢/lb.	105.0	103.4	-9.2
ALUMINUM (6/29) ¢/lb.	59.8	60.5	-17.4
WHEAT (6/29) #2 hard, \$/bu.	2.93	2.97	-11.7
COTTON (6/29) strict low middling 1-1/16 in., ¢/lb.	77.55	79.49	-3.1

Sources: London Wed. final setting, Chicago mkt., Commodity Research Bureau, Metals Week, Kansas City mkt., Memphis mkt.

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (6/28) S&P 500	371.75	377.39	4
CORPORATE BOND YIELD, Aaa (6/28)	9.04%	9.05%	-2
INDUSTRIAL MATERIALS PRICES (6/28)	98.8	98.9	-4
BUSINESS FAILURES (6/21)	368	383r	29
REAL ESTATE LOANS (6/19) billions	\$405.6	\$405.3	7
MONEY SUPPLY, M2 (6/17) billions	\$3,404.1	\$3,398.8r	3
INITIAL CLAIMS, UNEMPLOYMENT (6/15) thous	431	448	20

Sources: Standard & Poors, Moodys, Journal of Commerce (index: 1980=100), Dun & Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. CIBC seasonally adjusts data on business failures and real estate loans.

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
CONSTR. SPENDING (May) annual rate, billions	\$403.1	\$406.6r	-9
PERSONAL INCOME (May) annual rate, billions	\$4,778.9	\$4,755.1	3
CONSUMER SPENDING (May) billions	\$3,806.6	\$3,765.6	5
12 LEADING INDICATORS COMPOSITE (May) index	143.1	142.0r	-2

Sources: Census Bureau, Commerce Dept.

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (6/17)	\$860.7	\$856.6r	6
BANKS' BUSINESS LOANS (6/19)	309.9	309.5	-6
FREE RESERVES (6/26)	1,005	462r	57.8
NONFINANCIAL COMMERCIAL PAPER (6/19)	151.2	148.4	-0.5

Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed for a two-week period in millions).

MONEY MARKET RATES

	Latest week	Week ago	Year ago
FEDERAL FUNDS (7/1)	6.38%	5.90%	8.33%
PRIME (7/2)	8.50	8.50	10.00
COMMERCIAL PAPER 3-MONTH (7/1)	6.11	6.11	8.13
CERTIFICATES OF DEPOSIT 3-MONTH (7/2)	6.04	6.04	8.24
EURODOLLAR 3-MONTH (6/29)	6.08	6.05	8.25

Sources: Federal Reserve Board, First Boston

#Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment
1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful



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ARE THE WIZARDS OF WALL STREET CASTING MORE BAD SPELLS?

When I read in your story "Money machine" (Finance, June 10) that rocket scientists are again amassing tremendous wealth for themselves and their firms through various program-trading strategies, I wonder if this isn't just another shell game. The last get-rich schemes of the Wizards of Wall Street—junk bonds and highly leveraged mergers—certainly enriched Wall Street firms... but they came at the expense of many bankrupt companies and insolvent savings and loans, and the taxpayers ended up paying the bill.

What poor group of dolts and buffoons are losing billions of dollars by betting against these people? In a battle of wits against Wall Street, most banks, S&Ls, insurance companies, and pension funds show up unarmed. Can your reporters find out whose pockets are being emptied? Will it be mine again?

Ron Petersen
Boulder, Colo.

BUY IT OVER THE COUNTER, BUT STILL ASK YOUR PHARMACIST

Your recent article on prescription medications moving toward over-the-counter status ("Strong stuff—without a prescription," Personal Business, June 17) should have noted that Feldene is not an antihistamine but an anti-inflammatory agent. Because of errors such as this, patients should always consult their pharmacist before purchasing any over-the-counter medication.

This can prevent inappropriate use and possible interactions with prescription medications.

Leslie G. Epstein
Owings Mills, Md.

OVERSEAS SUPPLIERS MAY NOT HAVE CLEAN HANDS, EITHER

It is interesting to note that the companies Joan Neuhaus, the planning director at Archbishop Bergan Mercy Hospital in Omaha, decided to do business with are not lily-white either ("The gnat trying to sting an elephant can get GE,"

Top of the News, June 24). [Instead of avoiding General Electric Co.'s products on the basis of its nuclear weapons business,] she should have considered Toshiba's sale to the Russians of sophisticated machine tools, which can be used for the manufacture of ultrasilient props for nuclear subs. And let's not forget about Siemens and its involvement in research and development of nuclear power plants. Apparently, the folks at Infancia and Mercy Hospital didn't consider this.

It's always easy and socially correct to bash an American company. It's better to do business with foreign companies with similar practices. After all, we can see or hear what they do over there.

Sal Giordano
Appleton, Wis.

WHY FAMILY LEAVE DOESN'T BEAR LEGISLATING

In reference to the editorial "Family leave should get the nod" (June 17) comparing mandated family-leave legislation to the minimum wage, Social Security, and unemployment compensation is a lot like comparing apples and papayas.

While Congress has provided minimum labor and safety standards, it has always stopped short of dictating particular employee benefits. While most employees have vacations and pension and health plans, Congress has never mandated them. Minimum labor standards have been designed to help everyone. Mandated leave would not.

Mary T. Tavenner
National Association of
Wholesaler-Distributors
Washington

AL HAIG: OVERLOAD ON THE BOARDROOM CIRCUIT?

Your article "Al Haig: Embattled in the boardroom" (People, June 17) glossed over one key point. Haig, like many corporate directors, is simply over-committed. He has too many directorial and other business duties to serve shareholders well.

The average director of a large American corporation spends 108 hours a year per directorship. (Some estimates double that amount.) Haig, an average celebrity

BUSINESS WEEK
JULY 15, 1991 ***3222
ISSN 0007-7135



Published weekly, except for one issue in January, by McGraw-Hill Inc., Executive, James H. McGraw, 1221 Avenue of the Americas, New York, N.Y. 10020. Founder: James H. McGraw. President: James H. McGraw. Vice President: James H. McGraw. International Telephone: (212) 512-2000. Domestic Telex: 127990. International Telex: 127990. McGraw-Hill, New York, N.Y. 10020-1279. Copyright © 1991 by McGraw-Hill Inc. All rights reserved. Title registered in U.S. Patent Office.

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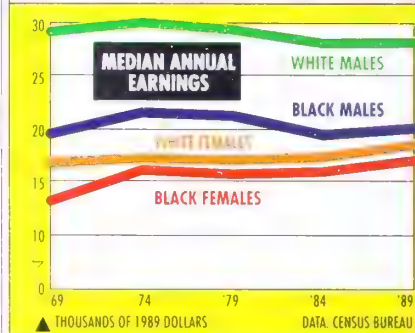
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Readers Report

CORRECTIONS & CLARIFICATIONS

The story "Pfizer finally sees its pay off" (The Corporation, July 1) contained an oversimplified estimate of Pfizer's potential liability from the Shiley heart valve. Shearson Lehman Brothers estimates there is a 90% probability that over a 10-year period the liability will be between \$80 million and \$270 million, and that there is a 10% probability it could reach \$800 million.

In a chart accompanying "Race in the workplace" (Cover story, July 8), line representing median annual earnings for white females and black males were transposed. Here is a correct version of the chart:



director, has a full-time job and four other current directorships. Thus, he spending about 432 hours (almost eleven 40-hour weeks) away from his full-time job. No wonder some companies believe that CEOs should not accept more than two outside directorships.

Jan F. van Ee
Stanford, Calif.

WHEN GAINS ON SELLING SHORT ARE PURE GRAVY

There is one point that was not discussed in "The long and short of short-selling" (Personal Business, June 10). Taxes are due when a short position is closed. In the case of a perfect short sale—a short on a company that goes out of business—no taxes are due.

That's because there is no offsetting closing trade. This is an example of where the astute investor wins and legally does not pay any taxes, a situation often referred to as a terminal short.

Gim P. Hor
Acton, Mass.

THE SAVINGS WERE 10 TIMES AS BIG

Your story "Mutual fear and loathing at a mutual fund" (Finance, June 17) comments on a lawsuit I recently brought against Mutual Series Fund

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Readers Report

Heine Securities (the fund's advisee and seven of the directors of the fund)

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Stanley A. Kitzinger
Haworth, N.J.

A FRESH BATTERY—AND WIPE THE WINDSHIELD, WOULDJA?

After reading about quick-charge batteries for electric cars in "Ni san jolts Detroit" (Top of the News June 3), I came up with a suggestion. Why should a driver worry about recharging his battery? Why keep the same one when it is empty?

In addition to service stations supplying gas for regular cars, why not have them keep a supply of recharged batteries to trade for empty ones?

A quick disconnect, switch, reconnect payment—and the motorist is on his way. The limited range would be offset by the two-minute replacement time, versus several minutes for filling a gas tank.

Ronald J. Adams
Rochester, N.Y.

THE KUWAIT SHERATON IS TAKING FALL RESERVATIONS

In "A vote at the U.N. doesn't mean a check in the hand" (Top of the News June 10), your caption stating that "ITT Sheraton lost a management contract" may have been misleading. When Kuwait was invaded, the Iraqis took over the hotel. So, quite clearly, our management contract was "lost" during this period. But throughout the seven-month occupation, our relationship continued with the Kuwaiti owners.

Soon after the liberation of Kuwait City, we began coordinating the necessary repair work and can report that the Kuwait Sheraton Hotel is now expected to reopen for business in September.

Pamela Hanlon, Vice-President
ITT Sheraton Corp.
Boston

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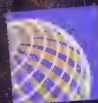
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BULLS IN THE CHINA SHOP: AND OTHER SINO-AMERICAN BUSINESS ENCOUNTERS

By Randall E. Stross

Pantheon • 330pp • \$25

A BILLION CUSTOMERS, A THOUSAND BLUNDERS

George Bush argues these days that China's trade privileges with the U.S. should be renewed to promote political reform there. "I don't want to be the President that isolates China," is his refrain to a Congress angered by China's stance on human rights, arms sales, and trade abuses.

Can trade links change a nation's politics? The question applies to Eastern Europe and South Africa in the wake of reforms, and to the coming debate over lifting the U.S. embargo on Vietnam. But it is especially pertinent to China, where from 1979 on, businesspeople have outnumbered—and had more influence than—any other Americans, including diplomats and teachers.

Bush's stance is contradictory: He hopes to bring down Hanoi's Communists by denying aid and trade yet claims that sustaining business with China will speed the downfall of Beijing's hardliners.

Randall E. Stross, who has studied U.S. business ties with China over the last 20 years, is less equivocal. In *Bulls in the China Shop*, he writes: "We usually do not treat

businesspeople as merchants of ideas, but... we find American businesspeople and their Chinese counterparts meeting at the intersection of culture and ideology." Predictably, the relationship has been mired in misunderstanding. But the political impact on China has been profound. Seeing foreign executives fight for sales, confront the party, and take responsibility on the shop floor has given many Chinese a new idea of what an individual's role and privileges can be.

Chinese-American business encounters have often been more like collisions, says Stross. His book is filled with examples involving Coca-Cola, RCA, American Motors, Occidental Petroleum, and dozens of other pioneers.

Americans and Chinese doing business together have faced deep-seated cultural differences. Arbitration of contracts is a case in point. One U.S. company found the Chinese unwilling to negotiate un-

less the Americans promised no legal action would follow. At heart was each side's notion of the bilateral "friendship" that had been toasted from Beijing to Washington. "Friends," said the Americans, stick to firm agreements. "Friends," said the Chinese, don't sue.

Americans managing Chinese have been tripped up often and hard by such differences. The manager of the Shenzhen International Hotel told workers to treat the hotel as their home. They did—pilfering food, cutlery, and linen.

Early on, says Stross, Americans who

On U.S. business' misguided romance with the China market, the book damning. As Stross presents them, the first U.S. executives in China, enthralled to be doing business in such a remote and novel land, forgot the wisdom gained elsewhere overseas. Envisioning an untapped market of a billion innocents incapable of corruption and ignorant of commerce, many were drawn into commitments and losses they would not have tolerated elsewhere.

As the veil lifted, U.S. salespeople learned what the CEOs had missed in their three-week tours: The Chinese system was complex and corrupt. Delay and evasions were grounded in strategy, not ignorance. Contracts were the start, not the end, of real negotiations.

Moreover, the objective of Deng Xiaoping's "Open Door" clashed outright with U.S. hopes. The party elite wanted only one thing, technology. They didn't wish to change the essence of their socialist system, say Stross, but rather to make it flexible enough to accommodate Western knowhow.

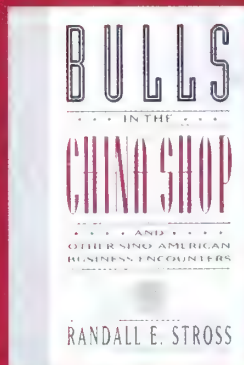
His more optimistic conclusion is that welcoming U.S. business moved China toward reform. In our hope that the Chinese would become more like us was naive, the Chinese nonetheless had to rethink their system to modernize it. New hotels needed new management and incentive systems and work ethics that challenged socialist ways. Enterprises made financially autonomous needed capital, which led to stock issues, exchanges, and debate on the Marxist principle of state ownership of the means of production. The need to import technology challenged China's pride and prompted dissident attacks on Chinese culture.

Stross calls the tension between the Chinese and American systems "gargantuan, almost geological." And Washington's debate over China's most-favored-nation status has raised that tension higher than at any point since 1972. Stross has done a fine job of illustrating how Chinese-American relations stumbled to this point. Business readers may be flattered, or horrified, to realize what a key role U.S. salespeople, executives, and engineers have played in the drama that climaxed at Tiananmen and continues now on the floor of Congress.

BY DINAH LEE

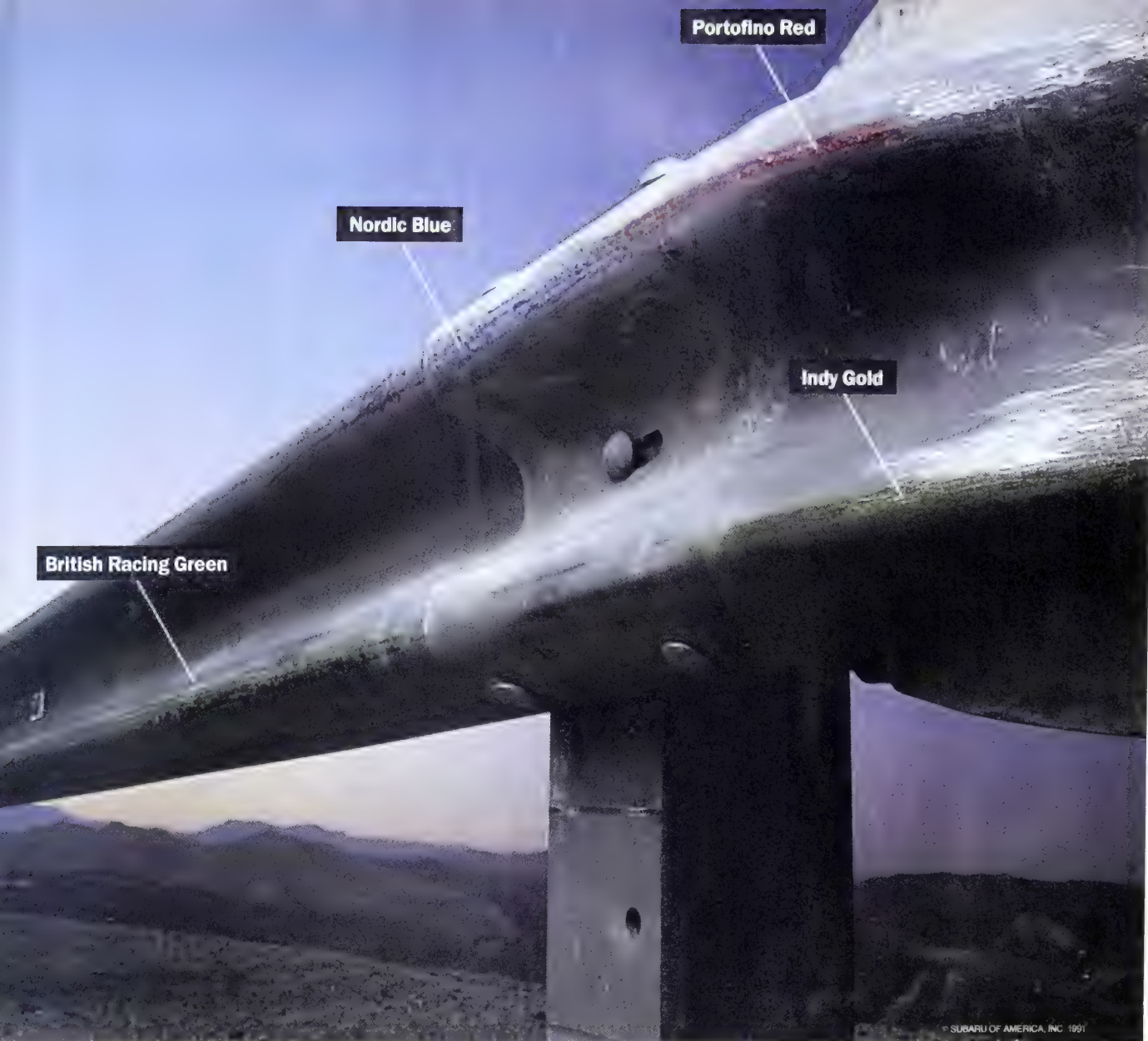
Hong Kong Bureau Manager Lee has covered China for 19 years.

Can U.S.-China trade, even badly mishandled, promote political reform? Stross says yes



had been fed negative images of China were so relieved that their hosts weren't villains that they abandoned their critical faculties. A Pullman Kellogg official gushed in 1979 that the Chinese never raised the possibility of bribes because they "aren't made that way." But by 1989, Boston businessman Garrison Rousseau observed that "the difference between graft in China and other places is that in China, you can't get things done even when you've paid bribes."

There are many comic moments in *Bulls*, but taken together, the tales have, as Stross writes, "a tragic quality." Since the Tiananmen Square massacre in June, 1989, it is the Chinese "most influenced by American people and ideas" who have paid the highest price. Economists, students, and managers willing to test market forces have lost jobs, status, and, in the case of hundreds of political exiles, their homeland.



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PUBLIC FUNDS FOR RELIGIOUS SCHOOLS WOULD BE NO SIN

BY GARY S. BECKER



Parochial schools frequently offer superior education. As for separation of church and state, public funds already go to church-sponsored hospitals, for example

President Bush has proposed giving private schools the opportunity to compete against public schools for taxpayers' dollars. Although some cities and states already have programs that provide limited funds to private schools, there is considerable disagreement over whether schools supported by religious organizations should be allowed to compete for public funds, whatever the plan.

Many people believe that including parochial schools would violate the separation of church and state embedded in the First Amendment to the Constitution, which begins: "Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof..." But I believe that public funds should be available to religious-supported schools, provided that they are available on equal terms to all private schools.

Constitutional specialists differ over exactly what James Madison and the other proponents of the First Amendment meant, although they clearly wanted to guarantee freedom of worship. I am no constitutional expert, but I take the view that the founding fathers appreciated the advantages of competition for religious ideas and beliefs and added this amendment to safeguard against the kind of established church that dominated England at that time. Those beliefs that best satisfied the spiritual needs of the people would thrive in an open competitive environment where there is no state religion.

This "free-market" view of the First Amendment implies that public funds could be spent on the secular activities of parochial schools if they have to compete against public or other private schools. It also helps explain an inconsistency: Many programs do allow public funds to go to secular activities of religious groups. For example, patients can use medicaid and medicare benefits at church-sponsored as well as other private hospitals. And any religion that meets very minimal criteria can qualify for nonprofit status and gain exemption from local property and other taxes and regulations.

There are also precedents for including religious-sponsored schools in an education voucher system where taxpayers pay the tuition at schools chosen by students. The post-World War II G.I. bill covers the tuition of veterans at parochial colleges and universities. College students who receive Pell grants, federally backed loans, and other public support can use them to attend religious-sponsored colleges.

Some U.S. Supreme Court decisions indicate that the judiciary will allow public funds to be spent on parochial schools. For example,

in *Mueller vs. Allen* in 1983, the court supported the constitutionality of a Minnesota law allowing parents to deduct their children's parochial-school tuition from their state income tax—clearly an indirect subsidy. Earlier decisions allowed public funds to subsidize the transportation of students to parochial schools and to pay for their secular textbooks.

Despite these decisions, there is still strong opposition to including parochial schools in an educational voucher program at the elementary and high school level. Some fear that students who attend parochial schools will be subjected to religious indoctrination. But a program could specify that no school would qualify for public funds if it required attendance at religious services or instruction in a particular religion. And public funds would be limited to secular subjects and philosophical aspects of religious studies.

Opponents of the inclusion of parochial schools also believe that it would increase the degree of segregation of students by race or creed. One important study, the book *High School Achievement* by James S. Coleman and his colleagues at the University of Chicago, finds that 90% of all students at Catholic high schools are from Catholic families. But they also show that these high schools are less segregated by race and income than are public high schools. Of course, parochial and other private schools that participate in a voucher or other school-choice program would not be allowed to discriminate in the selection of students on the basis of race, religion, or family background. Their right to exclude troublesome students could also be curtailed.

HIGH ACHIEVERS. If religious-sponsored schools were inferior, the educational advantages of including them in a school-choice program would be dubious. But the study by Coleman and his colleagues concludes that Catholic schools on average provide better education than public schools. Students from all races and family backgrounds score much higher on achievement tests than do comparable students from public schools, even though average spending per student by Catholic schools is a great deal lower. The advantage is especially large among students from less educated and poorer backgrounds. Catholic schools do better partly because they involve parents and the community more closely in school activities.

Sooner or later, the need to upgrade the quality of education available to the poor and middle classes seems sure to force many communities in the U.S. to include private schools in a choice program. It would be a shame to exclude religious-sponsored schools, which offer a superior education.

GARY S. BECKER IS UNIVERSITY PROFESSOR OF ECONOMICS AND SOCIOLOGY AT THE UNIVERSITY OF CHICAGO

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THE ECONOMY IS REVVING—AND PROFITS ARE SET TO TAKE OFF

The profit slump is over. A growing number of economists, whether of the anemic-recovery school or the strong-rebound camp, are confident that as the economy snaps back, a double-digit corporate earnings rebound isn't far behind (chart). "We expect corporate earnings will rise at a 20% annual rate during this year's second half," says Mark Zandi, economist at Regional Financial Associates Inc. Adds Edward F. McKelvey, senior economist at Goldman, Sachs & Co.: "Corporate profits may fall

cost-cutting and savvy inventory management helped stay any earnings carnage. Corporate inventory costs, for example, currently account for only 12.5% of corporate cash flow, compared with more than 25% just 10 years ago, says RFA's Zandi.

Other economists add that business is holding a tight rein on labor costs. So as companies step up production to meet increasing demand, profit margins will widen, fattening the bottom line, says Goldman's McKelvey. Adding to the earnings optimism is the two-percent-age-point drop in short-term interest rates during this recession. Since about half of all corporate debt matures in a year or so, lower rates could cut the corporate interest bill by some \$15 billion over the next year. And as profits rise, corporate spending usually picks up, which in turn will reinforce the economy's upturn.

move their more creative, higher-paid people elsewhere. New York, say Byrne and Shulman, will "retain its title as global financial capital—despite a current downsizing of the financial-services industry—supported as it is by a vast global and domestic base of business."

BETTING ON COMPANIES THAT TAME HEALTH CARE COSTS

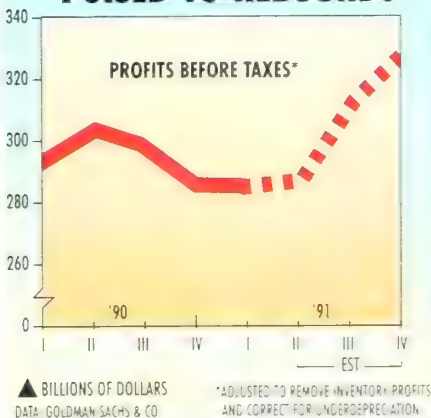
It isn't often that macroeconomists give stock market advice, perhaps for good reason. Not so A. Gary Shilling, head of his own economic-forecasting and investment-advisory firm. In a recent report, Shilling and his colleague recommend investing in the health care industry, specifically in companies that can capitalize on bringing escalating health care costs under control.

U.S. health expenditures are up from 6% of GNP in the early 1960s to nearly 12% in 1990. It has gotten so bad that national health insurance proposals are getting a serious hearing in Washington. But any fundamental reform is years away, the firm argues. In the meantime the system is evolving away from one with emphasis on high-tech medicine with little regard to cost, to one that offers basic care to individuals at a stable cost. To help investors make money off cost-consciousness, the Shilling report highlights a few efficient hospital management companies, such as Humana; outpatient-service providers such as Baxter International; and those companies, such as Novacare, that offer specialized rehabilitation services.

YOU CAN'T JUDGE A BANK BY ITS STOCK PRICE

Many economists believe the market is a good forecaster of what lies ahead for companies. Perhaps so, but in the case of troubled banks, it failed as a reliable early-warning system. That's the conclusion drawn from an analysis by economists Katerina Simons and Stephen Cross of the stock prices of 22 troubled bank holding companies from 1981 to 1987, which appears in the latest publication of the Federal Reserve Bank of Boston. Moreover, bank managers showed no systematic inclination to unload bank stock early on. Investors and management alike, say the authors, had to rely on bank examiners to sound the alarm that loan portfolios were deteriorating dramatically.

CORPORATE PROFITS: POISED TO REBOUND?



ARE IMMIGRANTS NEW YORK CITY'S SECRET WEAPON?

It is no great secret that many of the nation's cities are in dire straits. Adding to the long list of woes is a glut of empty office buildings. New York City is no exception, but according to Therese E. Byrne and David Shulman, analysts at Salomon Brothers Inc., the turn in New York City's fortunes is within sight.

They forecast that New York's office-vacancy rate could climb from a current 16.9% to nearly 19% by 1993 as the city continues to shed jobs—but then, its economy will revive as the layoffs taper off and the city's traditional wellsprings of strength emerge. And the commercial office market won't be far behind.

Entrepreneurial immigrants will jumpstart the local economy, as they have done so many times before, argue Byrne and Shulman. From 1984 to 1989, more than half a million immigrants settled in New York, about two-thirds of them from the Caribbean and Asia. Many of these immigrants are starting small businesses, a good number in the export and import trade. And other immigrants are successfully entering the work force, says Byrne.

Moreover, New York will keep its position as a gateway to the world economy. After all, it is cheaper for global companies to operate in New York than London, Tokyo, or Paris. And many foreign corporations, especially in the financial-services area, still find New York attractive. Indeed, many financial-services companies show little inclination to

short of the traditional rebound of 30% to 40%, but they are going to be much better than many expect."

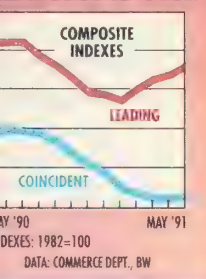
One reason the profit rebound may not match historical standards is that the downturn in profits was less severe than in most recessions. Pretax profits were down 4.2% in the first two quarters of the recession, compared with a 10.9% average decline during the last four recessions, says Stephen S. Roach, economist at Morgan Stanley & Co. On an aftertax basis, profits have done even better. These figures are for "economic" profits measured in the gross national product accounts, which are not the same as the profits reported to shareholders. Economic profits make adjustments to inventory and depreciation schedules as carried on company books to get a more exact picture of the overall trend in corporate earnings.

What accounts for the strength in profits? Overseas sales, for one. U.S. exports have been strong, even during the recession. For another, rigorous

THE RECOVERY MAY BE HERE, BUT HOLD YOUR APPLAUSE

American businesses and consumers can rest easy now: The White House has declared that the 1990-91 recession is over. Never mind that the downturn was under way for about eight months before Washington even acknowledged it. However, don't sit back and put your feet up just yet. It's still not clear if the economy's batteries are strong enough to keep a recovery going—let alone power a vigorous one. The Bush Administration doesn't have the final word, but the latest data make a compelling case. The government's chief forecasting gauge, the index of leading indicators, rose 0.8% in May. It was the fourth consecutive gain—a string that has always led to a recovery. More important, the index of coincident indicators, which plot the economy's present course, turned up in May for the first time since the downturn began in July, 1990 (chart). It rose 0.2%, after no change in April.

MORE EVIDENCE THAT THE WORST IS OVER



The coincident index—comprised of industrial output, employment, real income, and business sales—is instrumental in determining the peaks and troughs of the business cycle. As the numbers now stand, the index implies that the recession ended in either March or April. The June report from the National Association of Purchasing Management certainly suggests a return to the manufacturing recession. The NAPM's index of industrial activity jumped to 50.9% in June, from 49.1% in May (chart). It was the fifth consecutive increase, and a reading greater than 50% implies that the factory sector is now expanding instead of contracting. The NAPM said that production rose for the first time in a year, and that new orders posted the largest gain in 18 years. In addition, the government reported that factory inventories fell a steep 0.8% in May, to \$382 billion. And the NAPM said that its June index of inventories shrank to the lowest level since January, 1983. By keeping fewer goods on hand, manufacturers are ensuring that any increase in demand will translate almost immediately to a rise in output.

MONEY GROWTH COULD BE PROBLEM

If it were not for a lot of nagging questions, the recovery process from here on would be cut-and-dried. One of the biggest concerns is the inconsistency between a sick financial system and a healthy economy. Money still makes the world go round, but as of right

now, the growth of various measures of money and credit seems far below the pace that's necessary to fuel a lasting recovery.

Money was a major topic when the Federal Reserve's policy committee met on July 2. The central bankers not only set credit conditions for the weeks immediately ahead but also had to determine their targets for the growth rate of the money supply for 1992.

The Fed will disclose those objectives later in the month. Its current target range for M2, the most closely watched money measure, is 2.5% to 6.5%. M2 is presently growing in about the middle of that range.

However, 4.5% growth in M2 is very low compared with past recoveries. It is also troubling because faster money creation eventually translates into either economic growth or inflation. Set against the current 4%-to-4.5% pace of inflation, nearly all the expansion in M2 is accounted for by higher prices. That leaves almost no room for growth in real gross national product.

The only way real GNP can expand appreciably faster would be if money in the system were to turn over more rapidly. But history shows that money's turnover rate—or velocity—tends to fall in a recovery. The simple conclusion is that, unless the Fed allows a faster pace for M2, even a modest recovery—on the order of 3% economic growth in the first year—seems very doubtful.

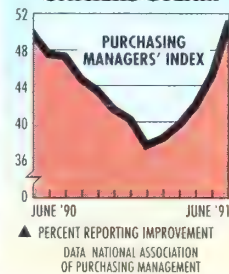
BANKS ARE LOATH TO LEND

The credit crunch in the banking system is only making matters worse. The current squeeze is not the classic variety but a hybrid brought on by increased regulatory scrutiny of bank loans, particularly for real estate, on top of banks' already shaky balance sheets. Those ledgers have been weakened by past bad loans, new capital requirements, and higher deposit insurance premiums. The result is an unwillingness of many banks to make the loans a growing economy needs.

During congressional testimony in June, Fed Chairman Alan Greenspan admitted that the central bank was still wrestling with the problem. Banks seem more willing to lend to home buyers and the U.S. government than to businesses. Bank purchases of Treasury securities are up more than 12% from a year ago, but many builders and others are being turned away.

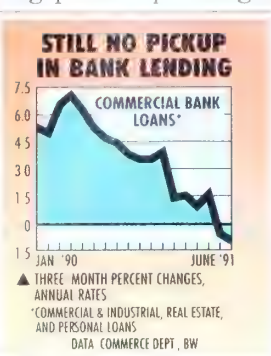
New rules on creditworthiness appear to be affecting

INDUSTRIAL ACTIVITY GATHERS STEAM



Business Outlook

a broad array of potential borrowers. The growth rate of loans for commercial and industrial purposes, real estate activity, and personal borrowing shows no sign of having picked up during the past three months (chart).



In fact, since March, aggregate loans in these sectors have fallen. That could reflect a weak economy, unwilling banks, or a combination of both. At any rate, it's not the kind of pattern you would expect to see from loan growth in a recovery.

The difficulty in getting loans is hurting builders, especially outside the housing sector. Total construction spending fell

0.9% in May, with outlays for new factories, offices, and other commercial projects falling steeply. In addition to the credit crunch, the oversupply of nonresidential buildings is another reason for the industry's problems.

Building contracts—a precursor of future construction activity—also turned down in May. They fell 5.3% to an annual rate of \$216.8 billion, according to McGraw-Hill Inc.'s F. W. Dodge Div. Total contracts so far this year are running 16% below their pace of 1990.

Despite the recent firming in housing demand, the Dodge report notes that past overbuilding of apartments and the problems in the banking system could dampen the strength of the housing sector's rebound. So the economy as a whole still cannot count on much support from the nascent recovery in housing.

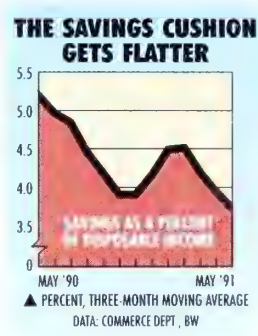
CONSUMERS SPEND, BUT WITH WHAT?

There is still plenty of doubt about the outlook for the consumer sector as well. Consumer spending last quarter increased three times faster than incomes. Given that earnings had fallen in each of the three previous quarters, such profligacy raises a serious ques-

tion: How are households going to finance their outlays this quarter?

Consumer spending jumped a strong 0.9% in May, after adjusting for price changes. The gains were fairly widespread, although big increases were posted in car buying and in electricity use during May's hot season. The weather caused earlier-than-usual buying of summer merchandise, however, which may have stolen some sales from June and July.

Consumer purchases are on track to rise at an annual rate of about 3.5% in the second quarter, a sign that overall GNP growth will be in the plus column. But income gains haven't been nearly as stellar. Personal income increased a strong 0.5% in May. But after taxes and inflation, second-quarter earnings are only growing at slightly more than a 1% annual rate.



Little wonder, then, that households are dipping into their rainy-day funds. Savings as a percent of disposable income fell to 3.6% in May, down from 4% in April and 5.3% a year earlier (chart).

Personal income will take another hit in July. That's when most new state and local taxes kick in, because July 1 marks the beginning of most states' fiscal years.

Tax hikes will shrink take-home pay at a time when savings are low and credit is hard to get for many households. That's why consumers will be unable to keep up their rapid pace of buying during the third quarter.

The tax squeeze, added to the financial problems of sluggish money growth and the credit crunch, make it hard to see the economy revving up for a robust rebound. The White House may say the recession is over, but the lethargic pace of economic growth in the coming months won't make it feel like much of a recovery.

THE WEEK AHEAD

INSTALLMENT CREDIT

Monday, July 8

Consumer installment credit in May probably increased by about \$1.5 billion, according to the consensus expectation of economists surveyed by McGraw-Hill Inc.'s MMS International. That would follow a \$1.7 billion advance in April. Prior to April, installment debt had fallen for four consecutive months. May's strong rise in consumer spending suggests that households expanded their revolving credit, and a slight pickup in car sales in May probably fueled auto loans. Monthly gains in installment debt had slowed sharply during 1990 and early 1991, and increases of less than \$2 billion per month are small compared with past re-

coveries. With income growth still sluggish, consumers are likely trying to pay off old loans before taking on new debt.

PRODUCER PRICE INDEX

Friday, July 12, 8:30 a.m.

The MMS consensus projects that the producer price index for finished goods settled down in June, rising a slim 0.1%. The PPI in May had jumped an unexpectedly large 0.6% because of several one-time price hikes. Producer prices, excluding the food and energy sectors, are expected to post a likewise modest gain of only 0.2%. This core rate of inflation had slowed to 3.6% during the year ended in May, from 4.1% in January. And there remain no signs of price pressures at the earlier stages of production.

RETAIL SALES

Friday, July 12, 8:30 a.m.

The economists in the MMS survey expect to see a 0.5% increase in retail sales in June, half of the 1% advance posted in May. Car buying provided some lift. Sales of both domestic and imported autos rose to an annual rate of 8.4 million in June, from 7.9 million in May. Gains elsewhere were likely held back by lower gas prices, which reduced revenue at gasoline stations, and by strong sales in May, which stole some purchases from June. Unusually hot weather in May accelerated purchases of summer items. Excluding cars, June retail sales are expected to show a rise of 0.4%, after a 0.9% gain in May.



ABB 1991

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A NEW WORLD DISORDER?

THE LONDON SUMMIT MAY WIDEN SOME RIFTS

George Bush likes nothing better than to trumpet his vision of the post-cold-war era. But when he arrives in London on July 14 for his annual meeting with leaders of the seven largest industrial nations, the President will have to confront the fact that his new world order may not be too orderly. The agenda for the London economic summit is suddenly overflowing with political challenges.

Bloody civil strife in Yugoslavia will cast one shadow over the meeting. And with his pointed admonition to "stay tuned," Bush is clearly keeping open the option of another military move against Saddam Hussein, perhaps a U.S. air strike against Iraqi nuclear facilities. But those hot spots are just the beginning. Bush's biggest problem could well be the political and economic impact of the summit's most celebrated walk-on, Soviet President Mikhail Gorbachev.

Indeed, the Soviet Union's role in the meeting is dramatically complicating things for Washington. Most important, the diminished military threat from the Soviets denies Bush a tool for whipping the Group of Seven allies into line on economic issues. "In the past, it made sense to solve economic and trade differences to avoid imperiling the overall security alliance against the Soviet Union," says C. Fred Bergsten, director of the Institute for International Economics. "Now, the end of the cold war really increases the risk of economic conflicts."

And there are plenty of conflicts—particularly over trade. The worst fear is that the London summitters will repeat the "go-your-own-way" approach that marked last year's meeting in Houston.

Then, allies glossed over disagreements on cutting farm subsidies—a dodge that backfired six months later when the Uruguay round of multilateral trade talks broke down because of the issue. "We're all haunted by Houston," says a senior Canadian official. This year, the outlook for resolving the farm subsidy conflict is no brighter.

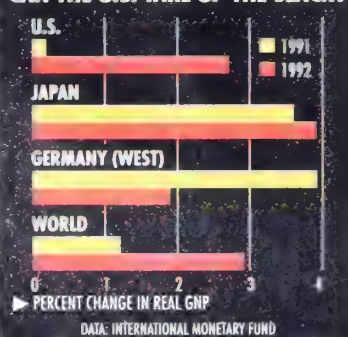
STUBBORN RATES. Nor can the G-7 leaders take much comfort in the prospects for world growth (chart). Bush will assure the summit that the U.S. has pulled out of its 11-month recession. But Washington will remind its allies that the global economy will remain sluggish unless they decide to pitch in—preferably with interest-rate cuts.

That campaign got an unexpected boost on July 1, when the Bank of Japan cut its discount rate a half-point, to 5.5%. The move reflected Governor Yasushi Mieno's concern that the latest Tokyo Stock Exchange scandal risks further undermining Japan's sagging equity market. Even more important, Mieno wants to be sure that Japan's nearly five-

year growth spurt continues. Still, chances for more rate cuts soon are dim. "Mieno isn't trying to stoke the fires of the economy," says economist Paul A. Summerville of Tokyo's Jardine Fleming Securities Ltd. "He's just trying to keep them warm."

Japan's modest action isn't likely to placate Treasury Secretary Nicholas F. Brady, who wants Germany to follow suit. With inflation rising and the mark falling as reunification outlays explode, the Bundesbank has steadfastly refused to cut interest rates. But with several European countries already in a slump, Washington fears that continued tight

GLOBAL GROWTH
CAN THE U.S. TAKE UP THE SLACK?



THE G-7'S FIVE BIG CHALLENGES

GORBACHEV

The Soviet leader's presence skewing the summit away from economic agenda and toward Moscow's reform woes. Meanwhile the G-7 lacks consensus on conditions for providing aid to Gorbachev's





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INTEREST RATES

Treasury Sec-
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G-7 partners—par-
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sion with interest-
rate cuts. But
Germany, beset by
unification woes,
won't budge. And a
U.S. recovery may
undercut Brady

EXCHANGE RATES

Europeans fret
that the strong
U.S. dollar will
feed inflation and
force interest rates
up. But the U.S.
won't accept a
firmer lid on the
greenback

TRADE

Failure to shift the
Uruguay round of
multilateral trade
talks out of neutral
could jeopardize
the global trading
system. Leaders
need a break-
through on U.S.-
Europe farm subsi-
dy issues

DATA: BW

money will undercut U. S. exports, which are fueling the American recovery. Says a senior U. S. official: "High European interest rates dictated by Germany aren't very good for world growth."

With little unity in store on the economic outlook, the last thing the summiteers want is a major distraction. But that's precisely what they'll get when Gorbachev rolls into London for a July 17 meeting with the G-7 and a private lunch with Bush. Gorbachev will be "the eighth member of the London summit," says Kazumasa Kusaka of Japan's Ministry of International Trade & Industry. The result in his view: Western leaders "will spend disproportionate time" groping for a unified approach toward the Soviet leader, who plans to renew his call for money and technical advice.

The White House isn't thrilled about Gorbachev's scene-stealing potential. To deflate some of his demands, Bush will challenge the Soviets to show that they're serious about rebuilding their shattered economy. Those close to Gorbachev say he'll respond by promising to create a market economy, including private property rights. He'll agree to liberalize foreign-investment rules. And Soviet officials say he will bring a list of defense factories ready to convert to civilian production with the help of Western companies.

'NO MONEY.' Those promises won't get Gorbachev much. At Bush's insistence, the G-7 will probably limit aid to specific help for a few targeted projects, including energy development, assistance in rebuilding the country's food-distribution system, and the conversion of those defense factories. Moscow can also expect associate membership in the International Monetary Fund, which could pave the way for IMF technical advice.

What cash does flow to Moscow will come largely from Europe. The U. S. is willing to allow the European Bank for Reconstruction & Development to open its spigot a bit—but not to the tune of billions, as the French and Germans would like. The West may also set up a currency-stabilization fund to help moderate Soviet inflation next year, when Gorbachev plans to turn the ruble into a convertible currency inside the Soviet Union. Even so, there's no chance that the sums will approach the Marshall Plan scale proposed by a Harvard-Soviet team (page 26). "The West is saying, 'This is a beautiful program, start fulfilling it,'" says Oleg I. Ozherelyev, personal economic adviser to Gorbachev. "But there is no money."

The Administration hopes that the horse-trading will at least give Gorbachev the political boost he needs to press

Top of the News

for reform at home. "It's not that Gorbachev wants to leave London with a check," says one senior U.S. official. "But he needs to be able to say that if Moscow moves to radical reform, the West will be there to back it up."

Gorbachev's high profile in London will almost certainly muffle the pleas for help from Eastern Europe. The U.S. had hoped to use the meeting to pressure

Western Europe into importing more farm products from the East. But the European Community, true to its stance in the Uruguay round, is resisting. There isn't much hope that restrictions will be lifted on textiles or steel, either. "It's just bad luck that their exports are precisely in industries that are very sensitive," says a top EC aide.

In the end, little may be settled at the

London summit. Indeed, with foreign policy dominating the meeting, Western leaders won't have much time to devote to economic discussions. That may leave the G-7 wondering if Bush's new world order isn't as contentious as the old one.

By Bill Javetski, Mike McNamee, and Douglas A. Harbrecht in Washington, and Rose Brady in Moscow, Blanca Riemer in Paris, and bureau reports

THE THINK TANKS ARE ROLLING INTO MOSCOW

As a guest of the conservative Heritage Foundation during Boris Yeltsin's recent trip to Washington, Vladimir Shumeiko made all the usual stops on the capitalist tour. He walked past Georgetown's trendy boutiques. He went to a suburban shopping mall. He toured a Safeway supermarket.

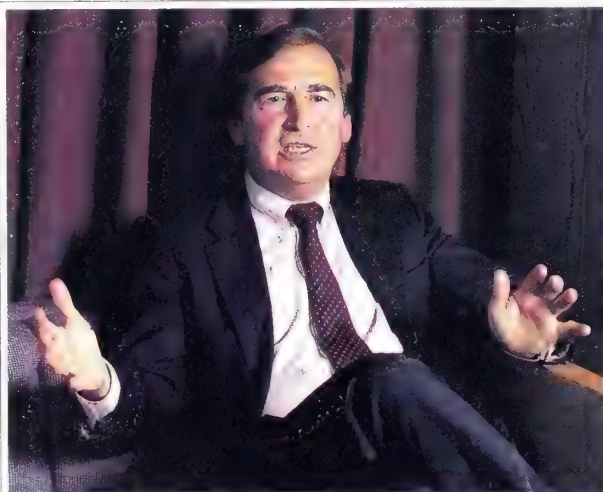
Shumeiko, an elected people's deputy of the Russian Republic, did something more serious as well. He rolled up his sleeves at a series of think-tank seminars on the nitty-gritty details of privatizing coal mines, converting military plants to civilian use, and mobilizing capital to dismantle 70 years of a communist economy. "From theory we're switching to practice," he says. "Economic reform is now a war of laws."

If Soviet squabbles over the country's economic future look like a battle, U.S. academics are only too happy to enlist. While Western leaders grapple with Soviet President Mikhail Gorbachev in London, economists, political scientists, and advice-givers from Harvard to Stanford are elbowing their way into the Soviet economic debate. They are consulting with the Kremlin and the governments of Soviet republics, exchanging visits with Soviet lawmakers, and drafting new laws on property ownership. The Soviets contribute some expenses, but the big payoff for the American think tanks is that their efforts give them an edge in the competition for U.S. foundation grants.

ABOUT-FACE. Advice is coming from some peculiar places, such as conservative U.S. think tanks that only recently were pondering the Soviet threat. The Indianapolis-based Hudson Institute, for example, made its reputation in the 1960s by positing that the U.S. could win a nuclear war. Now, it's doing an 18-month study to guide the Baltic re-

publics of Lithuania, Estonia, and Latvia toward a market economy. And in April, Stanford University's Hoover Institution agreed to advise Yeltsin's government on how to carry out a rapid transition to a market economy.

Edward P. Lazear, a University of Chicago economist and a member of the Hoover team, says that a plan for privatizing slaughterhouse operations through worker buyouts was virtually translated into Russian law from Hoover papers. "We're almost like congressional aides to them," he says.



HARVARD'S ALLISON: HIS PLAN TIES AID TO SOVIET REFORM

But for now, Harvard University's John F. Kennedy School of Government is the star of the go-go Soviet-advice business. A team led by Kennedy scholar Graham T. Allison Jr. and Soviet economist Grigory A. Yavlinsky scored a coup by floating a six-year plan for a "grand bargain" that would offer massive Western aid in exchange for Soviet reforms, such as liberalizing prices. Neither the Soviet nor Western governments have shown more than polite interest in the plan, but it could weigh heavily over the London summit.

Although the Bush Administration blanches at any big aid proposals, officials say they found the Harvard effort

useful. For one thing, Harvard's tally of hefty dollar commitments made the Administration's modest plans for offering Moscow technical advice and trade credits look far less controversial, especially to the Republican right.

PR BONUS. The think tanks may be earning reams of publicity and a steady stream of grants, but there are risks, too. "There's a lot of money to be made in this area, but the idea that anybody in the West can provide the answer to the reform riddle is profoundly dangerous," warns one Administration Soviet expert.

Indeed, most U.S. think tanks, Kennedy included, lack deep expertise in the Soviet economy. Some critics claim that having institutions such as the Hoover work for republics can only exacerbate tensions between Yeltsin and Gorbachev. Some Washington officials fear that by talking about aid, think tanks will raise expectations among Soviets that can't be met. Soviet KGB chief Vladimir A. Kryuchkov even claims that U.S. proposals are a Central Intelligence Agency plot to infiltrate the Soviet hierarchy.

Such sensitivities have prompted the Bush Administration to quash some links. When the government of Estonia asked the State Dept. to arrange a Rand Corp study of security matters in the restive Baltic republics, alarms went off, since Rand does classified research for the Pentagon. The U.S. nixed the scheme.

There's another gritty reality, too. No matter what economic scheme U.S. academics dream up, the Soviets still face some very hard political decisions. Think-tank free-lancing in Soviet affairs may be on a fast track, but actual reform is still slow in coming.

By Bill Javetski in Washington, with Peter Galuszka in New York, Keith H. Hammonds in Cambridge, Mass., and bureau reports

A CONUNDRUM NAMED CLARENCE THOMAS

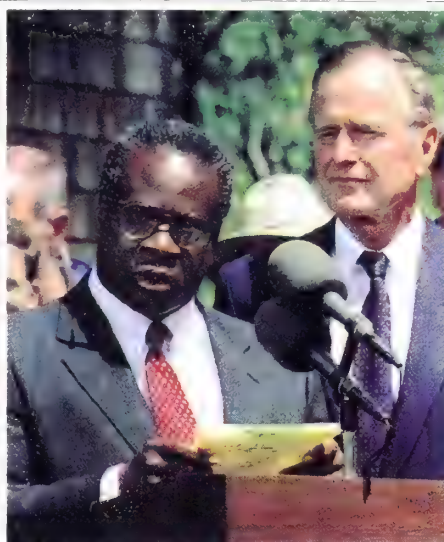
Bush's nominee will divide the Democrats—and likely be approved

George Bush didn't get to the White House by being a political naïf. He showed that again on July 1 when he picked a black conservative appellate judge, Clarence Thomas, to replace retiring Supreme Court Justice Thurgood Marshall.

It's a move that allows Bush to pursue a shrewd divide-and-embarrass strategy to win confirmation for the 43-year-old Thomas. It will be awkward for liberal Democrats on the Senate Judiciary Committee, who staunchly back the pending civil rights bill and affirmative action, to oppose a black nominee to the high court. "I love the prospect of Ted Kennedy tongue-lashing this black person sitting there below him," says Thomas Jipping, policy director at the conservative Free Congress Foundation.

AGONIZING. The nomination also is apt to split the Democrats. Some may attack Thomas' inexperience, since he sat on the federal appeals court in Washington for just 18 months. But Southerners, eager to satisfy two key constituencies, will gladly vote for a black conservative. For black political leaders, the choice is even more agonizing. Jesse Jackson is quick to criticize Thomas, an outspoken foe of affirmative action. But National Urban League President John E. Robinson was more equivocal. "Obviously, Judge Thomas is no Thurgood Marshall," he said. "But if he were, this administration would not have appointed him." One dilemma for Robinson and others: If Thomas doesn't make it, odds are that Bush would nominate a Southern white female or an Hispanic. Black leaders would then have to take the blame for leaving the court without a black justice.

Thomas is hardly an unknown quantity—as was David H. Souter when Bush



THOMAS: "I COULD NOT DARE DREAM THAT I WOULD EVER SEE THE SUPREME COURT"

picked him for the court last year. Thomas prefers individual rights to group rights. As Equal Employment Opportunity Commission chairman under Reagan and Bush, Thomas steered the agency away from hiring goals for minority groups, instead pursuing individual discrimination cases. The shift won him enemies among civil rights groups.

They led the fight against Thomas at his appeals-court confirmation hearings in 1990. The Judiciary Committee still approved him 13-1. But the stakes are higher now, with Bush and the Democrats locked in combat over civil rights. Still smarting from their Souter defeat, women's groups will pressure liberals to oppose Thomas unless he gives his views on abortion. Pro-choice forces fear that another conservative vote on the Rehnquist court could spell the death knell for *Roe vs. Wade*, the 1973 abortion-

rights ruling. Four justices have already signaled a desire to overturn *Roe*, and a challenge could come next term.

As a judge, Thomas has handled few constitutional cases. A preliminary review by the liberal Alliance For Justice found Thomas' rulings "do not indicate an overly ideological tilt," yet he's conservative on criminal issues. His inexperience could offer political cover to liberals looking to oppose him.

But the personable Thomas may disarm his detractors. Following Bush's announcement, he fought back tears twice when recalling his poor childhood in rural Georgia, where he was raised by his grandparents and spurred on by nuns at an all-black parochial school. "I could not dare dream that I would ever see the Supreme Court, not to mention be nominated to it," he said. He graduated from Yale law school in 1974, then worked as an assistant attorney general in Missouri and as a lawyer for Monsanto Co. Among his heroes: Malcolm X, who advocated black self-reliance.

SAILING THROUGH. To prevent slipups, the White House has already talked to GOP lobbyist Tom Korologos—who helped Souter—about coaching Thomas. Bush aides want to replicate Souter's masterful performance. During his confirmation hearings, the New Hampshire jurist deftly turned aside probing queries—and sailed right through.

Korologos figures Thomas' Achilles' heel is his youth. Democrats "look at him and realize they are going to be looking at him for 40 more years," he says. That prospect drives them crazy. Democrats haven't had a nominee since the Johnson Administration.

Between them, Bush and Reagan will have filled six of the nine Supreme Court seats if Thomas gets in. Bush may fill more on a court that has already sharply limited death-row appeals and civil rights, and upheld state curbs on abortion rights. Ultimately, the only brake on an ever-more-conservative court will be a Democrat in the White House. That doesn't seem likely soon.

By Tim Smart, with Douglas Harbrecht, in Washington and Michele Galen in New York

KEY ISSUES FOR THE NEXT TERM

ABORTION

The court will likely review one of a handful of new state laws that severely restrict abortion, taking the opportunity to address the 1973 landmark abortion-rights ruling, *Roe vs. Wade*

CIVIL RIGHTS

Should the 1954 school-desegregation ruling, *Brown vs. Board of Education*, apply to colleges? And how long should court-ordered desegregation plans remain intact? The court may rule

TOBACCO LIABILITY

The court will consider whether federally mandated health warnings on cigarette packs shield tobacco companies from state liability suits

ENVIRONMENT

Arguments will be heard on whether Congress acted unconstitutionally when it called a temporary halt to lawsuits over threats to the spotted owl

FIRST AMENDMENT

A decision is expected on whether New York's "Son of Sam" law violates free-speech protections. The law bars criminals from profiting from books written by or about them

DATA: BW

'JACK WELCH'S JACKHAMMER' NAILS A CORNER OFFICE

The former No. 2 at GE is taking his intense style to Allied-Signal

Lawrence A. Bossidy knows how to bide his time. After 34 years at General Electric Co., lately as vice-chairman, the 56-year-old executive recently turned down several top-notch corporate presidencies. He wanted the No. 1 spot. "Given my age and my experience, I didn't need any more training," he says.

Now, Bossidy has what he wanted. On July 1, he took over as Allied-Signal

Bossidy won't say much about his plans, except that he'll emphasize productivity. "I want to identify people who have passion, who are willing to make a commitment, take ownership, and make it a premier company," he says.

Allied-Signal's new CEO has been a leader-in-waiting for years. As No. 2 to GE's high-profile CEO John F. Welch Jr.—who calls Bossidy his best friend—the vice-chairman operated out of the

needed a \$25 million settlement with the government that forestalled a likely indictment and led Rudolph W. Giuliani then a U.S. attorney, to hail GE as a "responsible corporate citizen."

Still, Bossidy's intense style can be tough. "There's nothing subtle about the guy," says a former Kidder investment director. "You either deliver the goods or you're out." Under him, the pressure at GE is like "having to kill a lion every day," adds Nelson Gurman, general manager of GE's lighting operations in South America.

REGULAR GUY. Bossidy can turn on the charm, too. Employees say he is as comfortable with shop foremen as with government lawyers. In fact, until recently, Bossidy was renowned for rushing around buttoned-down GE with his shirt-tail hanging out. "He's a lead-by-example kind of guy," says Robert E. Koe, chief executive of Milwaukee's U.S. Leather Holdings Inc., who worked for Bossidy until 1984.

American Express Co. Chairman James D. Robinson III, who sat with Bossidy on a Presidential task force on trade, calls him "a top-notch pro, a doer." And U.S. Trade Representative Carla A. Hills, who worked with him on the task force, says he's "just first-rate."

Friends say his regular-guy style stems from his modest roots. A shoe-store owner's son from Pittsfield, Mass., the 6-foot, 1-inch Bossidy at first seemed headed for a pitching career in baseball. In 1953, the Detroit Tigers offered him a \$40,000 signing bonus straight out

of high school. His father nixed that plan, insisting on college. At Colgate University, he led the Red Raiders into the college world series, but an arm injury dashed his athletic hopes for good.

Staying fit has become a mission for Bossidy, a reformed chain-smoker. He lost his twin brother, sister, and father to heart disease and has been vigorously watching his health for a decade. A golfer, he boasts a handicap in the mid-teens, down from about 23 a decade ago. Hard on himself even about recreation, Bossidy complains that he hasn't "progressed enormously" on the links.

Odds are that Bossidy won't have a lot of time for golf now. Those who know Bossidy say he won't wait long to overhaul things at Allied-Signal. He has been patient long enough.

By Joseph Weber in Philadelphia and Lisa Driscoll in New Haven

LAWRENCE A. BOSSIDY

Chief executive and chairman, Allied-Signal Inc.

AGE 56

EDUCATION Colgate University, BA in economics, 1957

EXPERIENCE A career General Electric Co. worker, Bossidy started as a finance management trainee in 1957. His last job was a seven-year stint as vice-chairman. As part of 11 years of work in General Electric Credit Corp., Bossidy masterminded the creation in 1984 of General Electric Financial Services, which posted \$14.8 billion in 1990 revenues

DATA ALLIED-SIGNAL INC. NEW



of his chief executive after years of outgoing chief Edward L. Hennessy Jr. to retire early to make room for him. As part of the deal, Bossidy will land the chairman's seat in December—a full 12 months before Hennessy wanted to retire.

'GOOD OLD RELIGION.' Bossidy has his work cut out for him. Allied-Signal is a mix of diverse business units, from aerospace and automotive equipment to oil exploration and engineered materials. Some, such as defense, are slow-growers and need an overhaul: Last year, Allied posted just a 3.4% increase in revenues, to \$12.3 billion. Profits declined 12.5%, to \$462 million. "Changes now have to be in the context of productivity improvements, motivating people, getting back to good old religion," says analyst Anantha K. S. Raman, who owns investment firm Anantha Raman & Co.

But Bossidy gets credit for a lot more. In the early 1980s, he built up GE Capital Corp. Under his leadership, the unit's revenues rose from \$1.1 billion in 1979 to \$10.1 billion in 1990. And he fashioned \$14.8 billion GE Financial Services by grouping GE Capital with Employers Reinsurance Corp. and Wall Street's Kidder, Peabody & Co., in which GE acquired 80% ownership in 1986.

That \$600 million Kidder deal put Bossidy in the hot seat eight months after it closed, when insider-trading allegations against Kidder officials surfaced. But Bossidy's response was nimble: He engi-

neered a \$25 million settlement with the government that forestalled a likely indictment and led Rudolph W. Giuliani then a U.S. attorney, to hail GE as a "responsible corporate citizen."



WAUKEE'S SUMMERFEST: MILLER IS WOOLING YOUNG ADULTS WITH SPLASHY PROMOTIONS

THE SUDS CHURN: THE SOAP OPERA AT MILLER

...mming Lite, a new ad campaign—and changes coming at the top

The recent history of Miller Brewing Co. can be distilled down to one word: Lite. The savvy marketing Lite created a brand new niche and propelled Miller from a fifth-ranked regional brewer in 1973 to the No. 2 U.S. brewer today. The brand accounts for 15% of Miller's volume and more than 10% of its \$3.5 billion in sales. But Lite has gone flat, while more recent entrants in the low-calorie market are gaining ground (chart). Now, Miller needs to repeat its marketing miracle to prevent further erosion of the brand's share.

That's the likely first assignment for Warren H. Dunn, the front-runner to become Miller's next CEO. Charles W. Schmid, the brewer's senior vice-president for sales and marketing, was once a candidate to succeed Miller's current CEO, Leonard J. Goldstein. But Schmid's June 23 resignation leaves Dunn—a veteran of Miller's legal and administrative ranks—with a clear shot at the corner office. Yet Dunn, unlike previous Miller executives, has no hands-on marketing experience. A dramatic repositioning of Lite is under way, led by a new ad campaign, which Dunn will have to be a quick study.

The key word is "quick." BUSINESS WEEK has learned that Goldstein plans to retire in early February at 65. Executives at Miller and officials at its parent, Philip Morris Cos., say privately that Dunn, 56, will almost certainly be named Goldstein's successor before then. A Miller spokeswoman calls talk of Gold-

stein's retirement and Dunn's promotion "pure speculation," and both executives decline to comment. But Miller's powerful wholesalers are talking openly. "Warren is now the heir apparent," says Ronald L. Fowler, president of Mesa Distributing Co. in San Diego. "I'd be very surprised if he wasn't made CEO within the year."

LESS THRILLING. No wonder Miller's wholesalers, retailers, and ad agencies are abuzz. The next Miller *braumeister* will control a mammoth ad budget, estimated to reach \$195 million in 1991. Much of that will be spent on Lite, which on July 9 is set to air ads that drop the 17-year-old "tastes great, less filling" slogan and launch a new campaign cooked up by Leo Burnett Co. The tag line: "Miller Lite. It's it. And that's that." The campaign, which will pit Lite head-to-head against Budweiser's "King of Beers," aims to revive Lite by pitching it as a brew for all beer drinkers, not just those who are counting their calories.

Although beer sales overall are flat, Miller

can't blame industry doldrums for all its woes. Its first-quarter shipments fell an estimated 6.6%, according to Jerry Steinman, publisher of the newsletter *Beer Marketer's Insights*. Industry shipments declined 5.2%, largely because retailers and consumers had stocked up in the fourth quarter to dodge higher excise taxes. Even worse, Lite's supermarket sales dropped 10.5%. That's more than double the falloff for Coors Light and Bud Light.

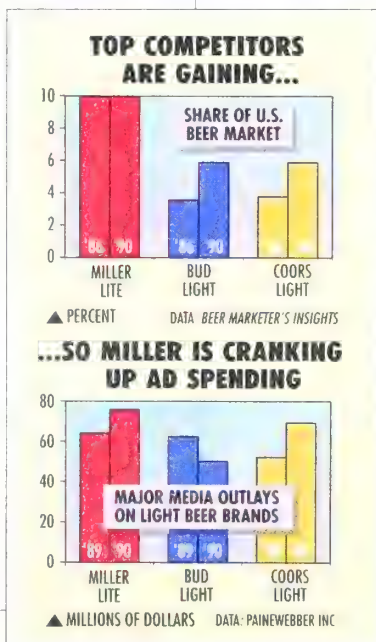
Even the shrewdest marketer would have trouble repairing the damage. And Dunn is a newcomer to the field. Following a stint at the Federal Bureau of Investigation, Dunn joined Miller in 1966 as assistant counsel. In 1984, he became senior vice-president for administration. Schmid, 48, was brought in at the same level three years ago. But late last fall, Dunn was promoted to executive vice-president, with Schmid and the marketing group reporting to him. "It was a surprise to us," admits Robert Lenz, recently retired president of Lite's former advertising agency, Backer Spielvogel Bates Worldwide Inc. "People thought Chuck was going to get it."

LO-CAL HERO? Dunn is already making his mark. In the nine months that he has overseen marketing, Miller has made a major push to put life back into Lite. In mid-March, it yanked the \$120 million Lite account from Backer and awarded it to Leo Burnett. Backer's "tastes great" campaign, concocted for the brand's 1975 rollout, "was so deeply imbedded in the American consciousness that it stopped having an impact five years ago," says Tom Pirko, president of industry consultant Bevmark Inc.

Burnett's new campaign targets younger drinkers. And Miller is wooing Coors' and Bud Light's young-adult crowd even more directly with a new product: Lite Ultra. Now in test markets, it has 77 calories, compared with 96 for Lite, 105 for Coors Light, and 110 for Bud Light. It's aimed at 21-to-30-year-olds, especially women.

Such brand extensions need distributor support. That helps explain why the reserved Dunn last winter donned a pair of bull's horns to amuse top wholesalers at a bash in Hawaii. "We'll do anything to sell a case of beer," he says. That includes taking a cram course in Marketing 101.

By Julia Flynn Siler
in Chicago



THE PHONE SYSTEM OF TOMORROW IS CAUSING MIGRAINES TODAY

And if the Bells don't get rid of the bugs, it could get worse

On June 26, more than 5 million customers in the District of Columbia, Maryland, Virginia, and West Virginia lost most of their local phone service for seven hours. The problem: A computer network that sets up calls went haywire, possibly because of a bug in its software. The same type of network was implicated in a major outage in Los Angeles on the same day. And in smaller outages in Pittsburgh and San Francisco a few days later. And in a memorable snafu in January, 1990, that crippled American Telephone & Telegraph Co.'s long-distance network for nine hours.

Beginning to notice a pattern? So are the telephone companies. But rather than reappraising the networks involved, all based on a design known as Common Channel Signaling System No. 7, the companies are actually planning to interconnect them in coming years—knitting together local, long-distance, and cellular phone companies more tightly than ever before. Some outside experts fear that doing so could allow problems to hop from one company's phone network to another, potentially bringing the entire national phone system to a standstill.

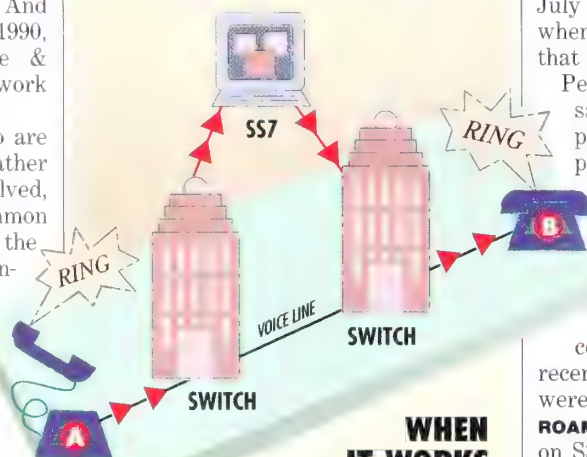
'BORDER GUARDS.' An outage that cascaded across networks would dwarf all the failures to date—and would be much harder to solve, given the likelihood of finger-pointing among multiple carriers with many brands of equipment. Michael Hills, president of HTL Telemanagement Ltd., a Burtonsville (Md.) consultant, calls Signaling System 7 “a disaster waiting to happen.” He accuses the phone companies of overreliance on centralized computer systems. Says Hills, whose own local service was knocked out on June 26: “This is a disease telephone engineers have, of trying to centralize things too much.”

That's an extreme view. The phone companies claim that they've designed filters that will allow only those messages that pass a slew of tests to go from one network to another, cutting the chance of a failure spreading between networks. Says AT&T spokesman James Messenger: “Each point of interconnect

will have border guards that are very efficient and very fast.”

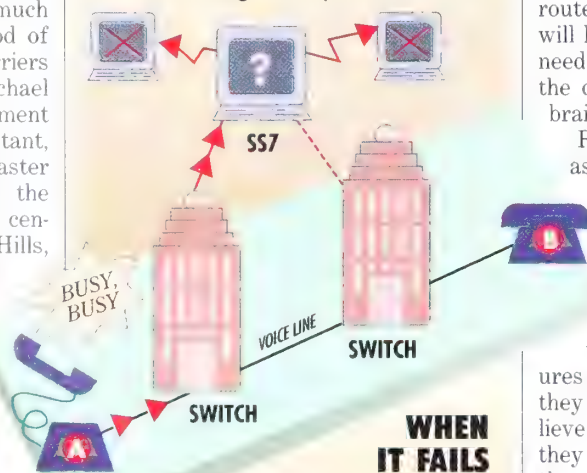
AT&T and other phone companies have a strong incentive to mend SS7: It allows them to use their networks more efficiently, saving hundreds of millions of

A NEW PHONE NETWORK



WHEN IT WORKS

A call signal from phone A is routed through the SS7 computer. It checks to see if phone B is free before linking them up on a voice line



WHEN IT FAILS

If one SS7 computer fails, others should take over. But if the software fails, too, the other computers could become overloaded. The result: system-wide meltdown

dollars a year. It also provides a high way for new services such as caller identification and advanced call-forwarding. In essence, it's a high-speed data network of signal-transfer points that overlays the traditional phone network. Electronic messengers race ahead to see someone's on the phone before a valuable circuit is wasted in sending the call through. The couriers can validate credit-card number stored in a database or look up how to route a toll-free call.

Such complexity breeds vulnerability. Investigators say the latest outages involved signal-transfer-point computer made by DSC Communications Corp. in Plano, Tex. Bell Atlantic Corp., whose mid-Atlantic network was creamed on June 26, says it's too soon to lay blame. Nevertheless, Bell Atlantic President Anton J. Campanella tweaked DSC on July 1, saying: “My tummy gets upset when a manufacturer delivers a product that doesn't work.”

Perhaps optimistically, Campanella says he still hopes Bell Atlantic can proceed with its industry-leading plan to tie its SS7 networks in three regions into those of a dozen long-distance carriers by year end. Meanwhile, BellSouth Corp. is testing SS7 links with McCaw Cellular Communications Inc. in South Florida. As it happens, cellular phones were spared in the recent outages—precisely because they weren't connected into SS7.

ROAMING EMPIRE. Carriers expect to rely on SS7 even more in coming years. The Advanced Intelligent Network of the future is to be built on a relative handful of computers that will know, for example, where customers are at any given time. SS7 will consult the computers and route calls accordingly. Phone customers will have one phone number for life and need never be out of touch. But if SS7 or the computers fail, the network will be brain-dead.

Raymond F. Albers, Bell Atlantic's assistant vice-president for technology planning, notes that phone failures were more frequent in the old days. Only then, they were far more localized—the result of a severed cable, say, or a fire in a switching center. With today's technology, network failures are rarer, but when they happen they can be doozies. While engineers believe that they can fix whatever ails SS7, they aren't making firm promises. “Notice a lot of us are using words like ‘should’ and ‘ought to’ instead of ‘will,’” Albers says. As networks become more dependent on computers, a lot of faith is being placed in fallible technology.

By Peter Coy in New York



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Salomon Brothers

Commentary/by Zachary Schiller

THERE'S STILL LIFE IN THIS RUST BELT RELIC

The boardroom of iron-ore giant Cleveland-Cliffs Inc. doesn't look much like a philosophical battleground. But there, on July 9, a strange event is set to take place. Seven incumbent directors are due to sit down for the first time with five new colleagues—all of them dissidents elected in May over management's strenuous objections. The newcomers say they have no special agenda. But if they should swing the \$310 million company around to their sponsor's way of seeing the world, Cliffs could become a prime example of the dark side of investor involvement.

The question confronting Cliffs is basic to a host of the nation's old-line industries: Should it invest in a future that may be essential to the common weal, even if it means a delayed or possibly even reduced return for shareholders? No question, the iron-ore business seems a natural candidate for what investment theorists call gradual liquidation, in which profits are paid back to investors rather than reinvested. It's old, it's dirty, and its customers—steel companies—have seen their best days. Yet Cliffs is convinced that its business could catch a second wind from well-placed investments. "In any mature industry, if you have a significant franchise, there's room to make money if you're good at it," says Chairman M. Thomas Moore.

BANG-UP JOB. The schism at Cliffs began as an argument over whether the company should funnel its cash board to shareholders or reinvest it in the business. Although impressed with Moore's record as an operator, 10% shareholder Tiger Management Corp. lacked confidence that the Cliffs board would invest wisely. So Tiger, run by renowned money manager Julian H. Robertson Jr., argued that management should begin a big share buyout.

Moore said no. He did agree in March to select a third of the board from nominees picked by Tiger but backed away. Robertson then fielded a slate of outsiders to run for the board on no particular platform. "Our only

agenda was to put independent, highly qualified people on a board that was not independent," says John A. Griffin, a Tiger managing director. That, Moore protests, was so much "veneer" for Tiger's real agenda: turning away from a long-term focus on the iron-ore business to pay out cash to investors. In any event, Robertson's slate attracted 42% of shareholders' votes, enough

offs and a special dividend have paid out the equivalent of \$8.35 a share since 1988, while the quarterly dividend has been reinstated—now paying 27¢ a share. Debt, at \$121 million, is a mere 32% of capital, and the company has nearly \$100 million in cash.

So what to do with all this new wealth? Moore looks at the sagging North American steel industry and takes comfort in his cash trove. He also figures steel's woes could provide the opportunity to pick up ore properties on the cheap. He sees a chance to grow abroad, too, where steel demand is expected to pick up, albeit slowly. Considerable industry investment is going into iron ore in Australia and South America.

'OPPORTUNITIES.' Further down the road, new technologies could allow Cliffs to supply iron in new forms to U.S. minimills, which have been growing at the expense of integrated mills. Cliffs and North Star Steel Co. are experimenting with substituting Cliffs' iron carbide for some of the scrap North Star uses. "There's a whole bunch of profitable opportunities around," says Firoze E. Katrak, vice-president for market assessment at consultant Charles River Associates Inc.

Not surprisingly, Tiger's view is as different as Wall Street is from Lake Erie. "Why would you ever want to invest in [mining] in Venezuela when you can buy in your own stock at six times earnings?" asks Griffin.

Moreover, Tiger doesn't trust Cliffs' incumbent directors, whom it characterizes as a clubby band too close to management. Griffin argues that shareholders have done well largely because a 1987 proxy fight squelched an ill-considered diversification that Cliffs' directors approved.

However, there's little to suggest that Moore is a free spender. He has focused on iron ore, and his track record suggests he may well be able to find profitable opportunities in it. The new directors, who say they have open minds about Cliffs' strategy, would probably serve shareholders best by giving Moore the chance.



A CLEVELAND-CLIFFS MINE IN HIBBING, MINN.

under the rules to win five seats on the board.

Curiously, even Tiger concedes that Moore and his team have done a bang-up job of rewarding investors since taking the helm in 1987. Back then, Cliffs was sinking into financial distress as its steel-company partners went bankrupt. But improved operations and healthier demand restored Cliffs to prosperity. Today, it accounts for more than 40% of North American iron-ore output and, though singed by the recession, is expected to earn about \$35 million this year. Moreover, spin-

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PHILLIPS PETROLEUM COMPANY 

TRAVEL



LATIN AMERICANS AT FLORIDA'S DISNEY WORLD, WHERE DOMESTIC VISITS ARE OFF

SUDDENLY, THE U.S. IS EVERYBODY'S OYSTER

The war is over, the dollar is cheap, and foreign tourists are flocking

At dusk, along Miami Beach's steamy oceanfront, a crew of multilingual waiters routinely scouts for foreign tourists to fill seats at a restaurant named A Fish Called Avalon. When maître d' Jack Donahue hears a group of tourists speaking German, a waiter moves in to translate the day's menu. It's a fruitful endeavor. "In the past month, business has been up 300% because of the internationals," says Donahue. "That has really helped our morale and changed our attitude."

The Persian Gulf war had depressed travel, but now foreign tourists are flocking to the U.S. in record numbers. By the end of 1991, some 42 million foreign tourists are expected to touch down in cities from Washington to Wichita—and to have spent a hefty \$57 billion. For the third year running, foreign tourism will generate more foreign earnings for the U.S. than such big-ticket exports as agricultural products and cars (table). Last year, foreigners spent \$3.1 billion more in the U.S. than Americans did overseas. As recession-crimped domestic travel limps along, foreigners will be even more important. "Foreign travel is sustaining the hospitality industry," says Michael Fisher, executive vice-president of Allied Tours in New York.

Few would have thought so six

months ago. When the bombs began dropping in the Mideast, foreign tourism plummeted. Fears of potential terrorist attacks emptied airports and hurt the tourist industry in many U.S. cities. In Los Angeles alone, would-be vacationers from Japan, Britain, and Germany canceled bookings at a 50% to 90% rate, according to the Los Angeles Visitors & Convention Bureau.

But tourists reappeared in time to witness America's victory celebrations. Arrivals at Miami International Airport, which dropped 13% during the war, rebounded by the same amount in late April and May, the latest months for which figures are available. Karl Fahr, chief of the U.S. Travel & Tourism Administration's Frankfurt office, says he expects a record 1.2 million Germans to travel to the U.S. this year. And London-based Thomas Cook Travel agency estimates that the number of British citizens

visiting the U.S. will top 1 million in 1991, a 25% increase over 1990.

The steady influx is timely for U.S. airlines. Saddled with big losses during the war, the airlines hope to load up with overseas passengers to cut some of the red ink. Continental Airlines says its Frankfurt-to-Newark route, which began on June 14, was 80% full. United Airlines reports that international flights are up 10% this year, while Delta Air Lines has added five daily flights from Europe. For the first time ever, American Airlines is advertising on European television and offering discounted fares in an effort to undercut European lines.

DOLLAR FEVER. Not all U.S. destinations have a cheery story to tell. In Orlando, Fla., home of Disney World, hotel occupancy rates are lagging, thanks partly to a decline in domestic visitors. O. J. Pizam, a tourism expert, Abraham Pizam, a professor at the University of Central Florida, says foreign tourists will not make up for the loss of U.S. guests "but will just keep it from being worse."

The main allure for foreigners is the cheap dollar. Although the dollar has strengthened in the past few months, the exchange rates are still favorable, and they encourage affluent foreigners to spend, spend, spend. Busloads of foreigners arrive regularly at the sprawling Tower Records in New York City and "they buy in quantity," says Jan Weaver, a supervisor in the record section. While the typical American spends around \$25, "sales can run \$200 to \$500 for a foreigner," she says.

The deepest pockets belong to the Japanese, who dish out seven times more than other foreigners on such goods as jewelry and clothes, according to the U.S. Trade & Tourism Assn. Tiffany in Vienna, Va., keeps special hours just for Japanese tour groups, who are even served breakfast, Japanese-style.

The rates are even making the U.S. accessible to less-affluent foreigners. Take Klaus Samstag, who was visiting Miami Beach with his buddies from Frankfurt. "I'm an auto worker, and he's a meat packer," says Samstag. "That's pretty ordinary, but now we can afford to come to America."

To encourage foreign travelers, U.S. resorts are more aggressively marketing to overseas tour operators, who book huge blocks of hotel rooms.

THE TOP CONTRIBUTORS TO U.S. FOREIGN EARNINGS

Industry	1990 sales Billions of dollars
FOREIGN TOURISM	\$51
AGRICULTURAL GOODS	40
CARS	37
CHEMICALS	36
CIVILIAN AIRCRAFT	32
COMPUTERS	26
METALS	23
CONSUMER DURABLES	21
TELECOMMUNICATIONS	10

DATA: COMMERCE DEPT.

ions, airline tickets, and tours. Walt Disney Co., which already has an office in London, opened a branch in Milan last year. And Anheuser-Busch Cos., the operator of four theme parks in Florida, recently hired a promoter in Frankfurt. The little guys are also vying for a piece of the action. After hiring a British public-relations firm, Ian Schrager is now producing television commercials to promote his Barbizon and three other New York hotels to travelers from France

and Britain. "Anything to generate foreign business used to be an afterthought," he says. "Now, it's a third of our budget."

But most foreign tourists already know where they want to go. The British head for Florida's beaches. The Japanese prefer Hawaii. The Germans are inclined to rent a car and drive across country. The Scandinavians prefer culture and shopping on the East Coast. Many are popping up in offbeat places.

Some Germans and French, who formed "cowboy and Indian" clubs, mosey over to Native American reservations. Indeed, the fastest-growing U.S. tourist destination is Kansas, according to the U.S. Travel & Tourism Administration. It no longer is necessary to export those amber waves of grain to rake in money from overseas.

By Antonio N. Fins in Miami, with Paul Magnusson in Washington, Andrea Rothman in New York, and bureau reports

RGY

WILL THIS BUBBLE EVER BURST?

The gas market is saturated—and low prices could last beyond 1993

Houston wildcatter Bruce Anderson figured he paid his dues in 1986—when crashing oil prices forced him to cut back production, lay off workers, and hang on for dear life. Since then, crude has rebounded nicely. But for Anderson, who looks to natural gas for 40% of his production, this year seems too reminiscent of 1986. This time, though, the bugaboo is gas prices, which have plummeted to their lowest level since 1972. In mid-June, gas-pipeline giant Columbia Gas System Inc. announced the low prices may drive it into Chapter 11, and Anderson is hunkering down. "It's a nightmare," he says.

Maybe for producers. But it's a dream for consumers. Spot gas, after kissing \$2 per thousand cubic feet (mcf) last December, in some areas is fetching less than \$1 per mcf—the oil equivalent of \$6 per barrel. The market is so saturated that the industry has abandoned its annual ritual of predicting an end to the gas "bubble," the surplus that has plagued the market for a decade. Now, even gas bulls see low prices lasting until 1993. And some gurus predict the glut will extend well beyond that (charts). Says Houston industry consultant Carol Freeenthal: "No one knows when it'll end."

SEE FALL. There's no rush, say big gas users such as utilities. Dual-fired generating plants can burn gas or coal, and less what they're buying these days. In May and June, Houston Lighting & Power Co. upped its daily gas purchases 50 million cu. ft., or 7.6%. The switch from coal saved \$45 million, which it's passing to customers. Other utilities are taking similar steps.

What a difference a year makes. After a freak warm winter stifled demand in early 1990, many producers hiked drilling; certain a normal season would re-ignite America's hunger for gas. In all, 140 new wells were drilled last year,

up 10.5% from 1989's 9,400, reports the American Gas Assn. But the weather turned warm again in January, leaving the system awash in supplies. An AGA survey suggests that newfound reserves, plus upward revisions to old fields, allowed companies to replace up to 120% of last year's production of 17.5 trillion cu. ft. (tcf). Producers that had been holding back supplies gave up and began flooding the market. After holding at \$1.78 per mcf in January, median spot prices tumbled to around \$1.30 for the rest of the first quarter—even though demand was up 7%, to 6.1 tcf.

Smaller players charge that the majors have aggravated the price slump by continuing to pump gas into a swamped market. Houston independent producer Anadarko Petroleum Corp. sought to shore things up by curbing output from its Matagorda Island facility in the Gulf of Mexico. But Anadarko says majority partners in the project, led by Amoco Corp., nixed the plan. "They're giving it away to keep market share," says a spokesman. In mid-June, prices fell anew—to about \$1.10 per mcf.

Columbia, a gas reseller, is the biggest

casualty so far—but small producers are also taking it on the chin. Stunned by falling prices, many have cut back drilling. Only 881 rigs are running in the U.S. today, vs. 1,021 a year ago, reports Houston oil-field service company Baker Hughes Inc.

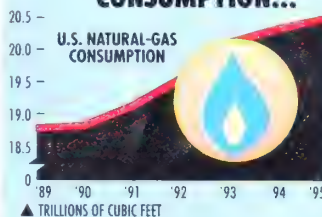
POWER DRILLS. Even a drilling slowdown may not cut the surplus by much, though. Power producers are signing more long-term deals—paying a premium for secure supplies. And that premium, anywhere from a few cents to \$1 per mcf over spot, may keep drilling fairly active. More gas is pouring in from Canada, which met some 7% of U.S. demand last year. Then there's a hefty tax credit for producing gas from coal beds, which adds to the glut. Benjamin Schlesinger, a natural-gas consultant, says that while prices could pierce \$2 per mcf in a cold winter, gas is so abundant they will average only \$1.50 to \$1.80 per mcf for the next few years.

If that's true, prices should still be high enough for all but the most marginal producers to survive. But there's little reason to expect a boom. A new study by Enron Corp., Houston, puts recoverable U.S. gas reserves at 1,000 tcf—50 years' supply. So as soon as markets start to tighten, the drilling rigs could rush back out and tap this vast reserve, driving prices down again for the second half of the 1990s. While that may cause bad dreams in the gas patch, it augurs well for consumers, who may be warming themselves with cheap gas for years to come.

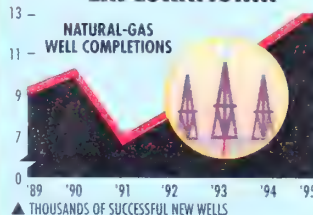
By Mark Ivey in Houston

A LOOK AHEAD FOR NATURAL GAS

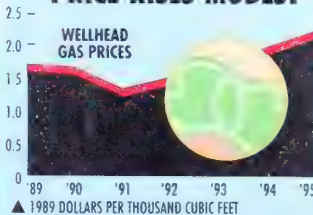
LOW PRICES ENCOURAGE CONSUMPTION...



...BUT STEPPED-UP EXPLORATION...



...SHOULD HELP KEEP PRICE RISES MODEST



In Business This Week

EDITED BY HARE

IBM AND APPLE: WIDER TALKS

► After a brief hiatus and a change of venue, Apple Computer and IBM got back to the table on June 29—and promptly expanded their discussions. They have worked out the preliminary terms of a deal that has them sharing microprocessor and software technologies. Now, say people with knowledge of the talks, the two are discussing co-development of a desktop workstation, a wireless network, and multimedia projects—the integration of video and sound with computer data. The multimedia exchange could alienate Sony, which has been working with Apple.

The talks were temporarily halted on June 25. During the break, hundreds of executives from both companies moved from IBM country in Austin, Tex., to Apple's home base of Cupertino, Calif. The deal, or parts of it, could be announced any day, those close to the two companies report.

AMGEN VS. J&J SCORE: 0-1

► Amgen lost the first round in its dispute with Johnson & Johnson and must pay that company's Ortho Pharmaceuticals unit \$164 million in damages. Amgen had licensed Ortho to sell its drug erythropoietin for uses other than kidney failure, but an arbitrator ruled that it had failed to help Ortho secure needed FDA approvals. Amgen, though, has outstanding claims against Ortho. Amgen charges that Ortho violated an agreement to help it develop two other drugs.

DEC PRINTS OUT A BATCH OF PINK SLIPS

► Bad news ahead for Digital Equipment's investors and employees. The computer maker is set to disclose on

July 8 that it's cutting as many as 9,000 workers from its work force of 122,000. The cuts, say Digital sources, will include the first major reductions in the 30,000-person sales and support staff.

Digital, which has already admitted that slow minicomputer sales may make cuts inevitable, confirmed that it's preparing a July 8 announcement to employees but declined comment on the actions planned. Wall Street analysts have warned that in the quarter ended June 30, the company could write off as much as \$300 million for layoffs and plant consolidations.

GE BRINGS GOOD THINGS TO LABOR

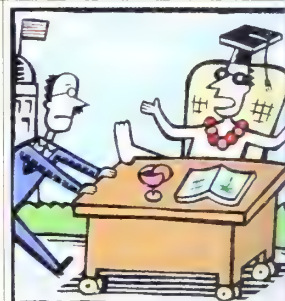
► General Electric has agreed to relatively generous terms in a tentative new contract with its two primary unions. The deal, which contains none of the onetime payments that GE's 65,000 union workers complained about in the 1980s, provides for pay hikes totaling 8% over three years. The raises, coupled with improved cost-of-living adjustments, mean that union workers will likely earn \$15.13 an hour by 1994, up 13.5% from today's average of \$13.33. GE also sweetened job-security and retirement clauses.

Employees, however, will have to pick up a larger share of medical costs. The benefit

AND DON'T WORRY ABOUT MISSING THE FINAL

Academics strive to become experts in their subjects. But George Harker seems to have gone a little too far seeking expertise in his. An associate professor who taught courses in the philosophy and history of leisure, Harker was fired on June 20 by Western Illinois University for, among other things, taking too much time off and being absent from teaching without a good excuse. One accusation: The professor was vacationing in Hawaii in late 1989 when he should have been teaching class.

Harker, an expert on nude beaches who frequently serves as a witness on the subject, says he was there to testify. But the Illinois board of governors sided with the university last month in an 8-0 vote, and Harker became one of the few academics to be stripped of tenure. When BUSINESS WEEK asked the university where the professor could be reached, a spokesman replied "The last we heard, he'd gone to Hawaii."



changes apply to all 200,000 people in GE's U.S. work force, including nonunion white-collar employees. Union members will vote on the proposed settlement on July 10.

VMS REALTY PAYS OUT JUST 7¢ ON THE DOLLAR

► It seems like a paltry return for the more than 20,000 people who invested \$1.2 billion in limited partnerships managed by VMS Realty Partners and sold in large part by what was then called Prudential-Bache Securities. According to a settlement approved on July 2, investors will split a

\$24.6 million cash settlement plus a small cut of future asset sales. That works out to perhaps 7¢ on every \$1 invested in the highly leveraged real estate investments that the Tax Reform Act of 1986 all but wiped out.

The payout breakdown is as follows: \$20 million from Prudential, \$1.1 million from VMS and \$3.5 million from Mutual Benefit Life Insurance. The former officers of VMS aren't required to contribute to the payout fund and are freed from personal liability for the VMS failures.

SEQUENT'S LOSS WAS NO GLITCH AFTER ALL

► For all the talk of a recovery, there's meager evidence of it in computers. On July 2, Sequent Computer Systems warned of a second-quarter loss "significantly" higher than the \$7 million first-quarter loss that analysts thought was just a glitch.

Sequent's problem: sharply falling sales of its large transaction-processing systems to Unisys, which resells them under its own name. As a result, Sequent is exiting the private-label business and will lay off up to 9% of its 1,700 person staff.



Datacomm Commentary

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we order UDS modems''

—Information Systems Group,
Wendy's International



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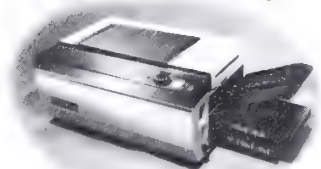
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LABOR AND THE DEMOCRATS: WITH FRIENDS LIKE THESE . . .

*I dreamed I saw Joe Hill last night,
Alive as you or me.
"But Joe," I says, "you're 10 years dead—"
"I never died," said he.*

—The Ballad of Joe Hill

Joe, if you're out there, it's time for you and the other union organizers of yore to check in with the home office. Strange things are happening on Capitol Hill, where Democrats hold sway and organized labor's legislative agenda usually gets a determined push.

No more. After years of seeing labor-backed initiatives get side-tracked in the Senate or squashed by a Presidential veto, Democratic leaders have given the AFL-CIO short shrift this year. The result: a stinging labor defeat over the U.S.-Mexico Free Trade Agreement and growing estrangement between union leaders and Hill Democrats.

HARD FEELINGS. Labor is particularly bitter about the defection of several Democratic leaders over the Mexico pact. Unions waged a fierce battle to deny President Bush "fast-track" negotiating authority, arguing that the treaty would result in massive U.S. job losses. But unions underestimated the allure of free trade. They lost by a wide margin, and the final tallies had Senate Majority Leader George J. Mitchell (Me.) and labor stalwarts such as Senator Edward M. Kennedy (Mass.) and House Majority Leader Richard A. Gephardt (Mo.) on the opposing side. The loss has driven a wedge between unions and Democrats. George J. Kourpius, president of the International Association of Machinists, attacks "elected 'friends' who go over to the other side when the political wind shifts."

The hard feelings don't end there. After the Mexico FTA,

unions' top priority is legislation that would bar employers from hiring replacements for strikers. But labor has managed to sign up only 33 Senate co-sponsors. Unions blame the poor showing on a tepid push from the Democratic leadership.

For some time, Democratic leaders have been trying to send the AFL-CIO a message: In a conservative era, the votes simply aren't there for many items on labor's legislative wish list. But labor's insistence on provoking down-in-flames showdowns has not waned.

What has declined is labor's political clout. As membership has fallen, business groups have become tougher foes, copying

labor's grass-roots-lobbying tactics. Younger lawmakers are more independent-minded than older pols. And President Bush's relish for the veto—which he has used to thwart labor-backed family leave and civil rights measures—means that Democrats need a hard-to-find 67 votes in the Senate to pass legislation.

What's labor's response to this mess? Petulance, mostly. The Machinists were so incensed by the fast-track defeat that they rescinded Gephardt's invitation to speak at their June 11 convention, and they vowed to deny campaign contributions



GEPHARDT'S VOTE ON THE TRADE PACT IRKED UNIONS

to other defectors. The Communications Workers of America plan to do the same to those who oppose them on striker replacement. The International Union of Electronic workers promised to go even further by campaigning against fast-track supporters. "If it hurts some people's feelings, tough," snaps IUE President William H. Bywater. "They are hurting us."

Labor and the Democrats aren't headed for a divorce—they rely on each other too much. But while they feud, prospects for parental leave, worker-safety measures, and other labor bills are fading—along with unions' legislative might.

By Susan B. Garland, with Paula Dwyer

CAPITAL WRAPUP

CENSUS

Even before the Commerce Dept. issued its 1990 census data in April, northern cities and states and minority groups had sued, charging that millions of people were missed by the original head count. The stakes were high since the census data affect everything from federal aid to the boundaries of congressional districts and, thus, political fortunes. But as a court-imposed July 15 deadline approaches, the Commerce Dept. to decide whether to make an adjustment, the steam seems to have gone out of the issue. Though Commerce is expected to reject an adjustment, the response from such

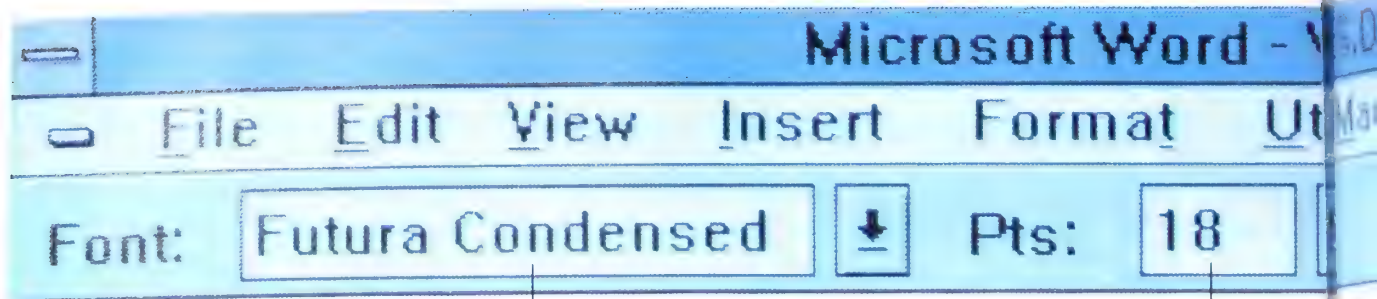
states as Michigan, Illinois, and New York, which blasted the undercount, may be muted. They now realize they wouldn't gain anywhere near as much from a revision as they originally thought.

TAXES

Bush Administration officials are floating the names of some high-powered economists for a commission to study the impact of a capital-gains tax cut. Among those on the list are former Council of Economic Advisers Chairmen Paul W. McCracken and Charles L. Schultze. But Democrats refuse to select their nominees, and the study seems dead for this year.

PEOPLE

Passed over again for the Supreme Court, Judge Edith H. Jones of the federal appeals court in Texas may still end up in Washington. Insiders are hinting that the former general counsel of the Texas GOP could be named Attorney General if Dick Thornburgh leaves. Jones has impressed Bush Administration officials and is backed by Secretary of State James A. Baker III. Jones once worked for his old Houston law firm. Thornburgh has said he'll run for the Senate from Pennsylvania, but his plans are on hold pending a ruling on the constitutionality of Pennsylvania's election law.

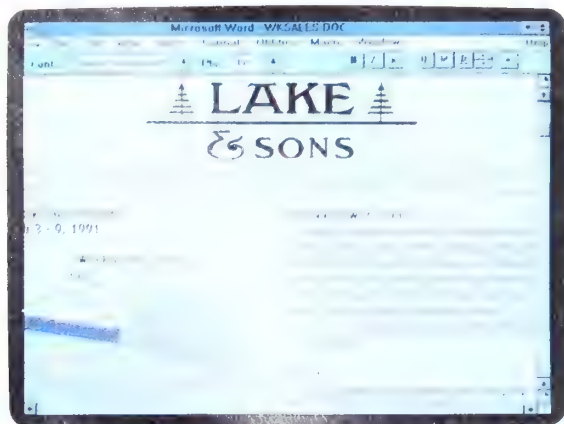


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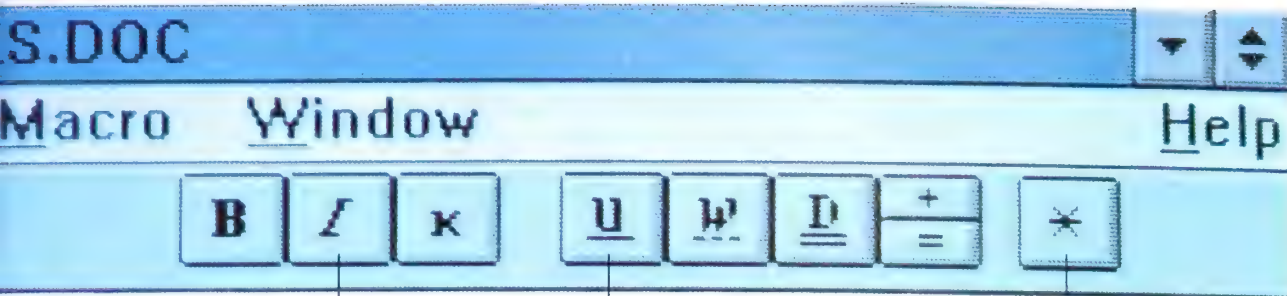


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'QUITE FRANKLY, BEING UNEMPLOYED STINKS'

As Europe's downturn grinds on, job cuts are hitting across the board

These days, Bill Goodliffe, a British truck driver, lives anything but the good life. Seven months ago, the 29-year-old was laid off. Unmarried, he manages to make ends meet by combining his weekly \$75 unemployment benefits with a little help from his folks. Every day, Goodliffe checks the bulletin boards at a local employment center for new jobs. But so far, no luck. "Quite frankly, being unemployed stinks," he says.

European companies are suddenly cutting workers at a furious pace. Goodliffe counts among the 900,000 Europeans who have lost their jobs in the past year, most of them in the past five months (chart). As Europe's downturn grinds on, the jobless toll in France is now at an all-time high, while unemployment in Britain is heading back to the disastrous levels of the mid-1980s. The job cuts are hitting people across the board: young and old, men and women, skilled and unskilled workers.

RUNNING SCARED. Even though the slowdown is relatively mild, except in Britain, corporations are making more drastic cuts than in past recessions. Most are running scared. The reason: They fear an onslaught of competition, especially from the Japanese, as the single market of 1992 nears. Says Bill Brodrick, a union official of the Transport & General Workers at Ford's plant in Halewood, England: "Everyone realizes only the fittest will survive." And few are con-

vinced that the modest 2.5% growth projected for Europe next year will be enough to merit new hiring.

This time around, there are no quick fixes. In past downturns, governments came to the rescue by pumping money into generous job-creation schemes. But as they move closer to monetary union, governments are unwilling to step out of line and take on huge deficits.

Hardest hit is Europe's service indus-

try, the engine of growth in the 1980s. That's especially true in Britain, where the advertising, banking, technology, and retailing companies that went on a pansion-crazy are now reeling. In the past year, British Telecommunications PLC cut its work force by 18,000, to 226,000. On June 2, clothing retailer Burton Group PLC, which burned millions on property development, sacked 1,600 workers and slapped a wage freeze on everyone else. Main streets in the once booming towns of southern England are lined with for-rent signs and shuttered retail outlets. Typical job seekers at British employment agencies such as Drake, Beam, Mori Ltd. are 40-year-old middle- or senior-level managers formerly earning \$62,000.

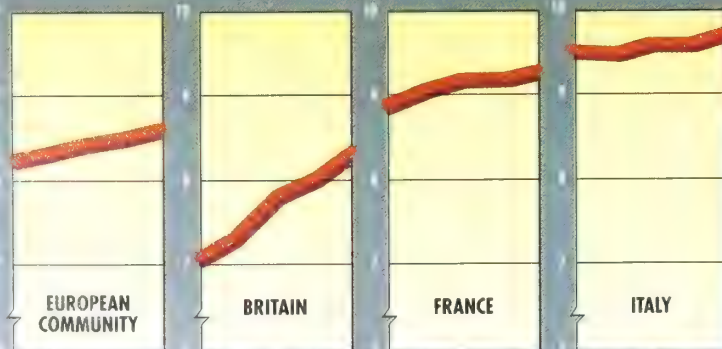
FURLOUGHS. Things are just as bad on the continent. Dutch airline KLM announced plans to trim 3,100 employees by February 1992, or 12% of the work force, readying itself for turbulence as the market deregulates. And with advertising revenue plummeting, Antenne 2, France's state-owned television network, just cut 377 jobs.

Europe's manufacturers, who thought the worst downsizing had passed, are also giving out pink slips. So far this year, 70,000 workers in the French auto, textiles, and electronics industries have been sacked. Auto parts supplier Valeo, one of France's growth stars of the late '80s, laid off 1,200 workers in February as car sales tumbled. Italy's Fiat has



ON THE STREET IN LONDON, PARIS, ROME...

UNEMPLOYMENT RATE



n furloughing thousands of workers week out of each month since September. With sales in Britain forecast to drop 22.5% this year, Ford of Europe is cutting production back to three days a week at its Halewood plant and may make some 2,000 job cuts. And facing a collapse in defense spending, British Aerospace PLC has trimmed its workforce by 23% over the past 18 months. Germany remains a special case. With 100 billion in government and private funds pouring into reunification, Germany has added some 700,000 jobs in the past year, half filled by easterners. But unemployment in the east is expected to rise at around 45% in coming months, threatening the country's overall unemployment figures to 15% (page 48).

As the jobless ranks swell, politicians are feeling the heat. In Britain, the Labour and Conservative parties are making employment a key election issue. They could. A staggering 23,161 British businesses collapsed in the first half of 1991, 1,900 companies are going out of business each week, according to Dun & Street Ltd. Prime Minister John Major is calling for a boost in vocational training, while Labor wants to require companies to pump 0.5% of payroll expenses into job-training programs. France's North African communities are growing tense, as youth unemployment skyrockets. Prime Minister Edith Cresson has made job creation her "first priority." Cresson wants to make professional training more efficient and bolster all enterprises.

DEEPEST CUTS. Fearing a political backlash, many governments and companies are beginning to get workers off the payroll without firing them. Dutch workers are not to qualify as disabled rather than unemployed to get better benefits. Philips Electronics has laid off some 10,000 workers worldwide in a restructuring plan to cut 55,000 from its workforce by yearend. Many Dutch employees will retire or go on the state's reduced payroll. Belgium's Generale Bank is trying to cut out 1,500 jobs through early retirements and attrition as it braces for stiff competition in 1992. And Italy's Fiat is relying heavily on *cassa integrazione*, a state-run system to lay off workers for a fixed period at 90% pay. Many argue that a leaner, meaner Europe Inc. is just what's needed to fend off such heavyweights as Japan's Nissan and Toyota in a single market. "We'll need a big increase in volume before we add workers," says Yves Crozet, director of finance at France's Renault. For labor that's bad news. And nobody knows that better than Bill Clinton.

by Blanca Riemer in Paris and Richard Melcher in London, with Patrick Oster in Brussels, and bureau reports



"WE'RE MAD AS HELL": A CLEAR MESSAGE OUTSIDE THE PROVINCE'S PARLIAMENT IN TORONTO

FOR CORPORATE ONTARIO, BOB RAE IS PUBLIC ENEMY NO. 1

The socialist premier's economic agenda has business seeing red

June 27 may be remembered in Toronto as the day business executives manned the barricades. As some 2,000 protesters from the construction, trucking, and other industries cheered outside the Ontario Parliament, the rally's organizer, John McBride, chief executive of Great Lakes Minerals, shouted: "We have a clear message for Bob Rae and his band of incompetents: 'We're mad as hell.'"

Until recently, Rae, who eked out a surprise win last September as Ontario's first socialist premier, had managed to maintain an uneasy truce with the province's powerful and conservative business community. But now that he's moving ahead with his agenda, the ceasefire is over. Already, the mudslinging is getting fierce. In a much-discussed newspaper column on June 25, one of Canada's most prominent executives, Conrad M. Black, CEO of Hollinger Inc., lambasted Rae as a "millionaire-baiting, anticorporate agitator" who is creating "conditions in which no rational person would invest a cent in Ontario."

While Black's views may be extreme, most Canadian CEOs are "very concerned" about the direction Rae is head-

ing, says Thomas P. d'Aquino, president of the Business Council on National Issues, Canada's leading business organization. Executives fear that Rae will drive industry out of Ontario, which accounts for 40% of Canadian gross national product and nearly half its manufacturing base. With the U.S.-Canada free-

trade pact a reality, there is more heat than ever on businesses to move to greener pastures.

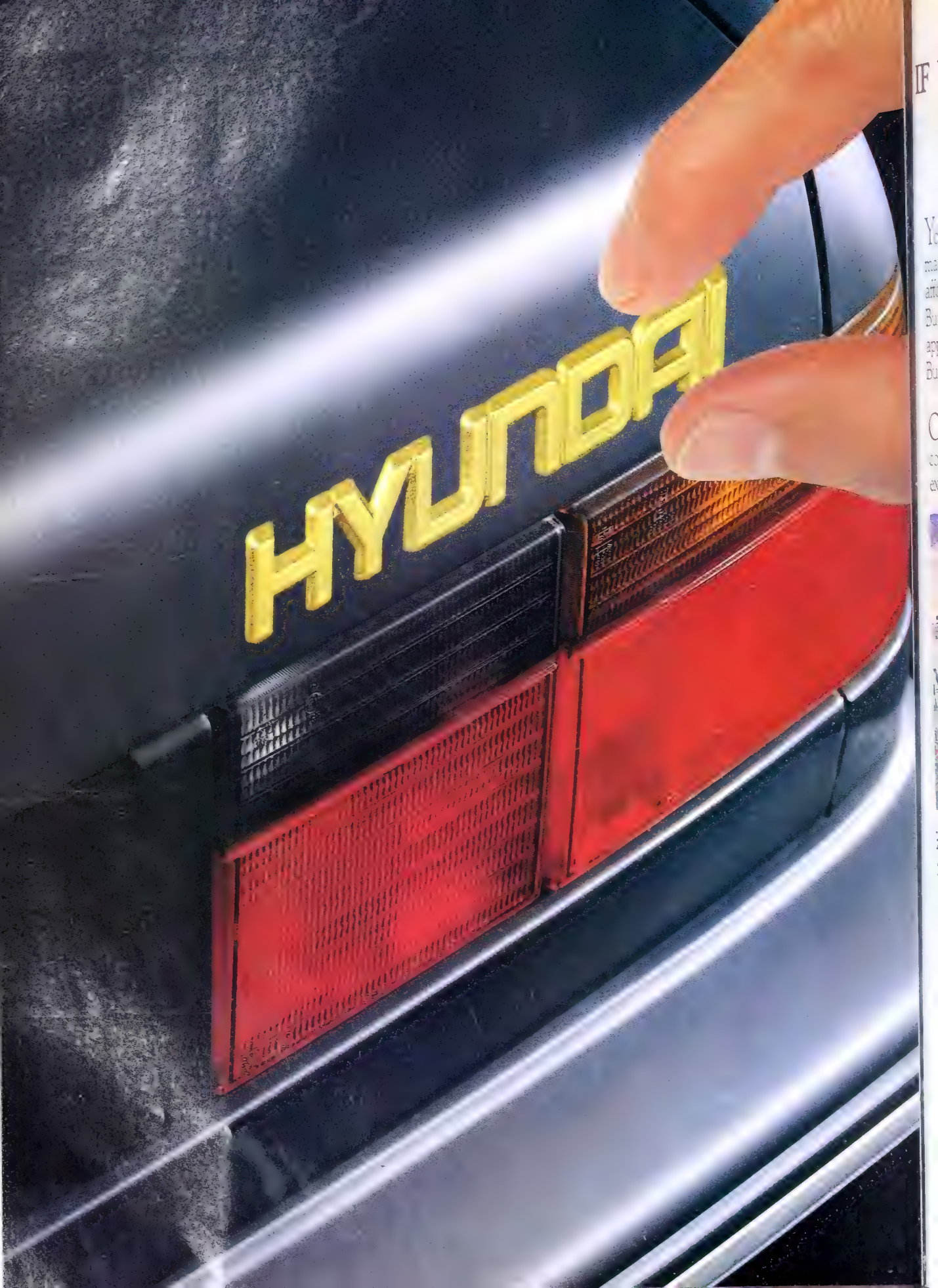
BUDGET BLOAT. What triggered the Toronto rally was Rae's budget for fiscal 1991, which calls for a startling 13.4% spending boost and a tripling of the deficit, to \$8.4 billion. Since the budget was unveiled in April, Ontario has lost its AAA credit rating. The big deficits projected for the next three years mean increases in Ontario's taxes, which are already among the highest in North America. And business fears that

Rae may soon sponsor pro-labor legislation and carry out past pledges to nationalize auto insurance.

The man Canadian business loves to bash is a 42-year-old lawyer who won a Rhodes scholarship to Oxford University in 1969. Rae says that working at a legal-aid clinic in the London slums con-



RAE: AN APPROVAL RATING OF JUST 21%



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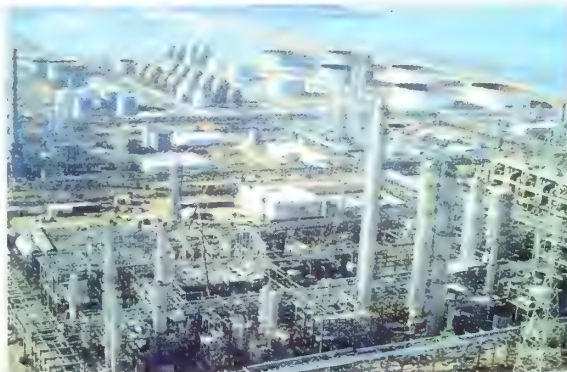
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firmed his leftist views. The Ontario boss of the socialist New Democratic Party (NDP) since 1982, Rae rode a protest vote against the worst recession since the 1930s and free trade with the U.S. to the premiership.

Under Ontario's parliamentary system, Rae, who doesn't have to run again until 1995, wields far greater power than a state governor in the U.S. But business leaders can make things hot for him. Already, their protests have helped cut the NDP's approval rating to just

21%, according to the latest Gallup poll.

Rae is enough of a politician to take heed. He eased up on plans to impose a big tax on gas-guzzling cars after loud warnings from General Motors Corp. and Ford Motor Co. of Canada. And he extended peace feelers on June 27, when he said he had "no interest in entering a four-year battle with the business community." But if the two sides fail to arrange at least a ceasefire, Ontario could become a war zone.

By William C. Symonds in Toronto

GERMANY

EASTERN GERMANY STARTS SHOWING A PULSE

Fresh capital, privatization, and a wave of startups are making an impact



THE BRANDENBURG GATE IN THE 1920s: THE BUNDESTAG'S MOVE MAY GIVE A LIFT TO THE EAST

In some respects, east Germany is a land frozen in time. In east Berlin, every weekday morning, thousands of listless workers emerge from bleak 1950s-style housing projects and trudge off to giant, belching factories. Once the showcase of the socialist system, these plants are nearing collapse. Subsidies from the west are all that sustains them.

But hints of change are in the air. In late June, the Bundestag voted to move the vast apparatus of government from Bonn in the prosperous west to Berlin in the heart of the blighted east. Many see the vote as a sign of determination to speed the turnaround of east Germany. "The decision for Berlin was an essential signal for the recovery of eastern Germany," says Daimler Benz Chairman Edzard Reuter.

The decision to move the government comes as Germany's very costly effort to remake the east's economy is showing signs of paying off, after a frustrating and painful transition year since reunification. The east's economy is getting some powerful medicine in the form of an incredible \$86 billion in government spending in 1991 alone. Private investors are kicking in another \$37 billion.

NEW JOBS. Most economists now believe the east's economy is hitting bottom, if only because it can't go much lower. While many more industrial plants face shutdown, services are starting to pick up. New building orders, for example, leaped to \$172 million in May, 50% above the total in April. One of the more optimistic forecasters, the German Institute for Economic Research in Berlin, now

says that gross national product will jump as much as 18% in the second half after declining 24% in the first half. "The negative things have already happened," says Heinz J. Hockmann, director of Commerz International Capital Management in Frankfurt.

The recovery in services and a few other sectors is creating jobs, offering at least some offset to continuing layoffs in heavy industry. Fresh investment and startups have so far added 1 million new jobs. Much of the demand comes from the core of new entrepreneurs. More than 340,000 east Germans have started new businesses, and banks have granted the startups \$6 billion in fresh credits.

At the same time, privatization has picked up steam. The Treuhand agency, the government unit for privatization, has sold 2,500 of the east's 9,000 former state companies and expects the total to approach 60% by yearend. For instance, Otto Bertz, CEO of Potsdam-based heating and plumbing contractor HVT, is scrambling to find workers and buy new equipment. Bertz, who just led a management buyout of the former state-owned company, plans to cash in on the expected surge of construction activity around the capital, just 22 miles away. He predicts a boom that will "radiate for 100 miles around Berlin."

BACKBONE. Beyond that, blue-chip companies are planning to move into or expand in the east. Sony Corp. just announced it will transfer its European headquarters from Cologne to Berlin. Daimler Benz is planning to double its 4,500 east German payroll by the end of the year. As megaprojects such as Daimler's get under way, many believe a backbone of smaller companies will form quickly. Large investors are already drawing medium-size suppliers to east Germany. Volkswagen's decision to invest \$3 billion in a new assembly plant in Zwickau and expand an engine plant in Chemnitz has brought seven new auto suppliers to the region, including France's Valeo, Britain's GKN, and Johnson Controls from the U.S.

But the first whiffs of an economic turnaround aren't much consolation to the hundreds of thousands of east German workers who are still facing layoffs between now and yearend as the government slashes payments to the 2 million "short-time" workers. Including the short-timers, who work half-days or less, unemployment will spike sharply this year, to as high as 4 million, or nearly 50% of the work force.

Unemployment at those levels can't be allowed to last long. But there is little more that the government can do. After pouring in money, it's moving itself to Berlin. The east Germans and private business will have to take over now.

By Gail Schares in Berlin

SALINAS NEEDS A LANDSLIDE —AND AN HONEST ONE

They may be the first elections a Mexican president ever really had to worry about. On July 7 and Aug. 18, Carlos Salinas de Gortari and his long-ruling Institutional Revolutionary Party (PRI) need to win sweeping majorities in countywide voting for Mexico's Chamber of Deputies, half of its state, and seven governorships. At stake are key elements of the proposed free-trade pact with the U.S., such as constitutional reforms on land ownership, that will need a two-thirds majority in Mexico's congress. And to ensure the choice of a like-minded successor when his term ends in 1994, Salinas needs to show his machine polls that his free-trade strategy gets votes.

Most PRI candidates are likely to win big. But for the first time, they may need to win honestly. If the PRI blatantly rigs elections, as in the past, it will give ammunition to U.S. free-trade opponents. Chances for approval of a trade pact by the U.S. Congress will be riding on opinions north of the border on issues ranging from Mexico's environmental mess to dirty politics. "There is some question of the credibility of Mexico as a partner in this economic marriage," says Rep. Don J. Pease (D-Ohio), a free-trade foe. "There's going to be a lot more focus on the political process in Mexico than ever before."

POLITICAL SHENANIGANS. In Nuevo León, a northern industrial state that the PRI has festooned with election banners, Monterrey Mayor Socrates Rizzo seems likely to win an early race for governor on July 7, even without cheating by the PRI. But winning fair and square may be harder for PRI candidates in the other Mexican states on Aug. 18, when the rest of the country votes. In the central state of Guanajuato, for one, gubernatorial candidates of the conservative National Action Party (PAN) and the left-of-center Democratic Revolutionary Party (PRD) are running strong. And in San Luis Potosí, the

PRD and PAN are backing a single opposition candidate. The loss of either state would create strains between Salinas and PRI political bosses. But the PRI could lose credibility if it rigs the votes, as it did last November in local elections in Mexico state, which borders on Mexico City. Party shenanigans there ranged from ballot-burning to migrating voting booths.

Opposition parties also complain that the Bush Administration, although it has made democracy an issue in relations with countries from the Soviet Union to Nicaragua, keeps mum about Mexico's shortcomings.

"There's no pressure from Washington [to clean up elections]," says Jorge Castañeda, a political analyst with close ties to the PRD. In the trade talks, the strong executive authority created by the PRI's political near-monopoly is an advantage for Salinas. It allows him to shape Mexico's negotiating position with little pressure from other parties and interest groups. But this is also a liability, says Luis H. Alvarez, president of the PAN, because "the executive cannot claim to be speaking for the entire nation."



THIS TIME, THE U.S. WILL BE WATCHING CLOSELY

Pease and 25 other U.S. congressmen hope they can remedy one complaint of Mexico's opposition parties: that Salinas and his coterie of technocrats have kept them in the dark about trade plans. The Americans plan to organize a two-day seminar in Mexico City in late July, giving politicians, intellectuals, and others a chance to discuss trade and related issues.

So far, Salinas has scored a political success by offering Mexicans a vision of the future that opponents can't match. The risk is that he shares responsibility with only a small group of collaborators. If his strategy falters, he could lose support within the PRI and open the 1994 presidential succession to rivals who don't share his vision. That would be a setback for Mexico's trading partners, too.

By Stephen Baker in Mexico City

GLOBAL WRAPUP

SOVIET UNION

Yes, there are unemployed in the Soviet Union—an estimated 2 million in Russia alone. After decades of official denials that Soviet joblessness exists, unemployment offices opened across the Russian Republic on July 1. A new Russian law allowing workers to register for unemployment benefits is a key step toward creating a social safety net that will be needed as the Soviet Union moves toward a market economy.

In Russia, economists predict, unemployment could grow to 12 million as enterprises lay off workers or go bankrupt. Jobless workers are entitled to a

minimum of \$73 monthly compensation for 12 months—about half the current average wage. But benefits can be cut for workers who turn down new job offers. Says Lydia Lezhova, director of a neighborhood unemployment office in Moscow: "Some jobs, like working as a mechanic, are considered not prestigious, even in the Soviet Union."

HONG KONG

By frightening off foreign bank financing, China has effectively blocked Hong Kong's \$16 billion airport scheme. Without Beijing's blessing, potential lenders consider the project too risky. As a result, the colonial government announced it will delay

work on the airport after nine months of bickering with China.

Many observers think the colony will be forced to scrap the controversial plan, which includes expressways, subways, and the world's longest suspension bridge. Mainland officials called the plan too costly and were angry at not being consulted on a project affecting Hong Kong's post-1997 finances.

Hong Kong's government is now exploring whether to sharply scale down its master plan for infrastructure. Some executives are calling for a small expansion of overburdened Kai Tak Airport. Construction of a new facility, they say, should be left to 1997, when China takes over.



Norm Goldberg, Digital

Bob Salipante, Ameritrust

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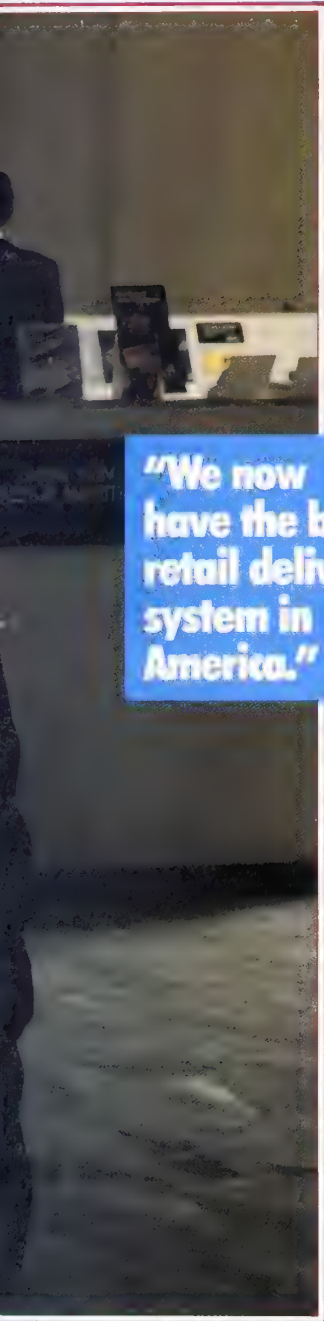
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A YEAR OF TWISTS AND TURNS

U.S. MARKETS SHINE AS JAPAN LOSES ITS LEAD AND EUROPE GETS PUMMELED

At first glance, it would appear to be sweet revenge on the Japanese corporate titans that have been beating up on their North American and European competitors. Results of BUSINESS WEEK's fourth annual survey of the Global 1000, which ranks the world's biggest companies by market value as of May 31, show more Japanese companies fell off the list than those of any other country. Moreover, the total capitalization of Tokyo's market fell beneath New York's for the first time since the survey began, the result of a 22% drop in the Nikkei stock average.

But look again. True, Japanese companies have lost market value. And the financial markets have been losing steam, most recently in the wake of the Nomura Securities Inc. and Nikko Securities Inc. brokerage scandals. But investors have turned the corner on the go-go 1980s, when they zeroed in on companies with real estate

and other inflated assets. Now they're concentrating on the fundamentals like never before. Notes Charles Elliott, executive director for international equity research at Goldman, Sachs & Co. in London: "The market has forgotten about assets and is going crazy over earnings."

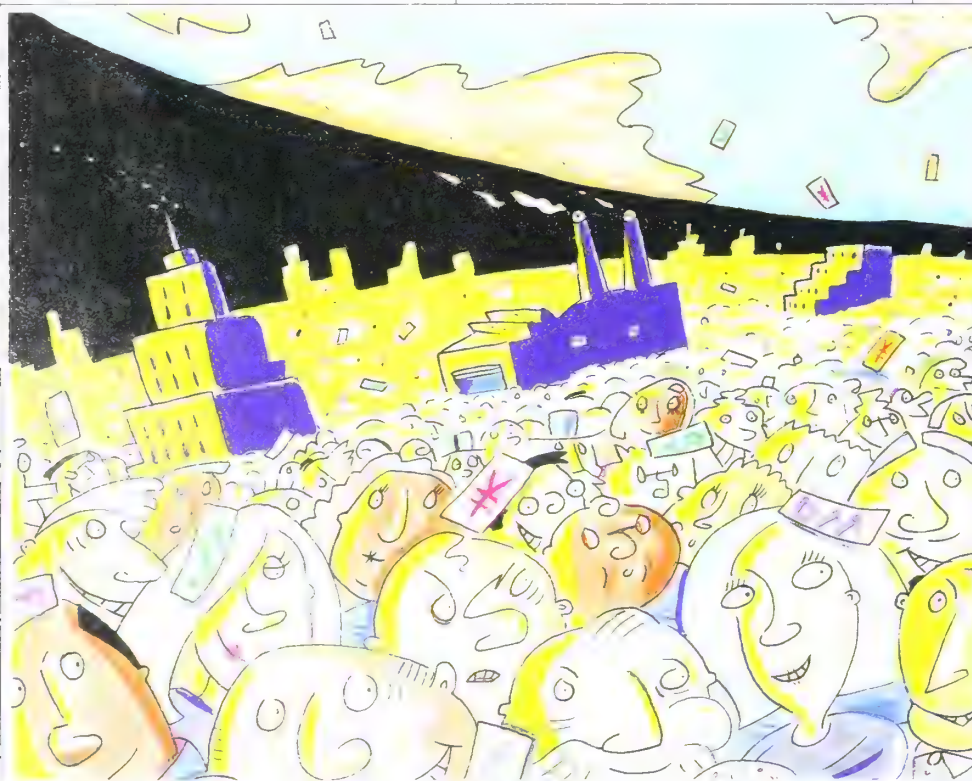
What investors see when they concentrate on the fundamentals is a strong Japanese domestic economy, which is creating a new set of winners. At the same time, Japanese exporters are gearing up for another boom. The renewed attention to high earnings growth and strong balance sheets is a reflection of how the country's underlying competitive muscle could emerge as formidable as ever.

That's just one of the twists and turns of this year's Global 1000. The times were turbulent: The invasion of Kuwait. The gulf war. Reunification of the two Germanys. A currency roller coaster. Stock markets

soared, or collapsed. As a sign of the times the total value of the Global 1000 was down slightly for the first time, to \$6.7 trillion, 0.2% less than in 1990.

FIRST IN, FIRST OUT. Compiled by Morgan Stanley Capital International in Geneva, the data base tracks 2,500 companies in 28 countries with developed markets. Country-by-country rankings follow the master list, shedding light on national trends. Standard & Poor's Compustat Services Inc. provides additional data on U.S. companies. And a separate table on page 103 ranks by sales and profits the top companies in South Korea, Taiwan, Brazil, and Mexico, whose equity markets restrict foreign investment or are relatively immature.

Although the Japanese showed underlying strengths, the Americans were far better investments this year. U.S. companies make up the entire list of the top 15 share price gainers. First to sink into recession



SALES

Billions of U.S. dollars

1. C. ITOH	\$152
2. MITSUI	150
3. SUMITOMO	144
4. MITSUBISHI	142
5. MARUBENI	141
6. EXXON*	116
7. NISSHO Iwai	111
8. GENERAL MOTORS	107
9. ROYAL DUTCH SHELL**	106
10. FORD MOTOR	97
11. IBM	69
12. TOYOTA MOTOR	66
13. MOBIL*	64
14. GENERAL ELECTRIC	58
15. BRITISH PETROLEUM	56

*Includes excise taxes

**Excludes excise taxes

ong the industrial na-
ns, the U.S. was also
first to see signs of re-
very. By May 31, the
w Jones industrial av-
ge, anticipating the re-
and, was up 15% from
first of the year.

Among the Americans
ders, tobacco and food
nemoth Philip Morris
s. moved into the top
even while faltering
M dropped a few rank-
s. Oil giant Exxon
p. took the No. 3 spot
bally. American phar-
ceutical companies also
cked big gains for in-
vestors, even though
re are trouble signs
ead (page 54). Wal-Mart
res Inc., with maverick
n Walton at the helm,
ned 52%, making the
ailer worth more on pa-
e than mighty Toyota
tor Corp. And a slew of
w companies made the
aking, from biotechnolo-

firm Amgen Inc. to Avon Products Inc.
Although currencies swung wildly
oughout the year, currency changes ac-
unted for little of the U.S. gains against
Europeans. Between May 31, 1990 and
y 31, 1991, the dollar rose 3% against
German mark, Europe's leading cur-
y. Meanwhile, the yen was up 9%
ainst the dollar in the same period, giv-
Japanese companies a slight boost.

MARKET GUIDE FOR INVESTORS

National composites of Global 1000 stocks

	Market capitalization Billions of U.S. dollars	P-E ratio	Yield	Return on equity
1. U.S.	\$2,559.3	22	3.1%	19.1%
2. JAPAN	2,346.6	60	0.7	8.6
3. BRITAIN	614.9	14	5.1	20.2
4. GERMANY	248.6	27	3.3	13.7
5. FRANCE	183.8	17	3.4	15.5
6. CANADA	119.3	27	3.5	10.0
7. SWITZERLAND	102.2	24	2.1	9.3
8. NETHERLANDS	94.1	12	4.1	38.9
9. ITALY	84.2	20	2.5	12.8
10. SWEDEN	68.7	21	2.7	14.4

DATA: MORGAN STANLEY CAPITAL INTERNATIONAL INC., BW



Stiff global competition and a downturn
hit European blue chips hard. France's top
companies suffered the most. Chronically
undercapitalized, they piled on debt after a
buying binge in the U.S. Glassmaker Saint
Gobain saw investors pull out to the tune
of 27% of its value, Paribas lost 30%, and
tiremaker Michelin dropped off the list.

German companies were only middling
performers, but with lots of cash and rich

banks behind them, they
don't depend on market
capitalization as much as
others. When the growing
pains from unification
ease, watch out for the
Germans. Still, carmaker
Volkswagen dropped 36%
of its market value, as
auto sales slumped across
Europe and the U.S. The
auto slowdown also clob-
bered Italy's Fiat.

NEW MOOD. Mired in re-
cession through most of
the year, British compa-
nies nonetheless benefited
from a strong stock mar-
ket. Big stalwarts such as
Grand Metropolitan PLC
and Guinness PLC gained
as investors fled to safety.
Retailer Kingfisher,
which owns the Wool-
worth's chain, added fully
51% to its market value.
Following the Anglo-Sax-
on pattern, Canada's mar-
ket was reviving by May
on hopes that its deep re-
cession was about to turn the corner. In-
vestors were particularly happy with tele-
communications giant Northern Telecom
Ltd., which gained a snappy 35% and
moved into the top quarter of the Global
1000. Even so, Canada's long-term pros-
pects are clouded by a decline in its com-
petitiveness, especially compared with its
southern neighbor.

But of all markets, the shifts in Japan

HOW THE GIANTS STACK UP

PROFITS

Billions of U.S. dollars

ROYAL DUTCH/SHELL	\$6.53
AM	6.02
EXXON	5.01
GENERAL ELECTRIC	4.30
BRITISH TELECOM	3.56
PHILIP MORRIS	3.54
TOYOTA MOTOR	3.19
BRITISH PETROLEUM	2.87
AT&T	2.74
PONT	2.31
EVRO	2.16
MURA SECURITIES	2.00
ILEVER	1.98
OBIL	1.93
MOCO	1.91

SHARE-PRICE GAIN

Percent from 1990, U.S. dollars

1. AMGEN	249%
2. U. S. HEALTHCARE	228
3. U. S. SURGICAL	197
4. NOVELL	131
5. COSTCO WHOLESALE	118
6. MEDCO CONTAINMENT SERVS.	110
7. THE GAP	104
8. FUND AMERICAN	102
9. CHIQUITA BRANDS INT'L	96
10. FREEPORT McMORAN C&G	81
11. PFIZER	79
12. MERRILL LYNCH	74
13. HOME DEPOT	63
14. NATIONAL HEALTH LABS.	63
15. IMCERA GROUP	63

RETURN ON EQUITY

Percent

1. GILLETTE	472.2%
2. LYONDELL PETROCHEMICAL	358.9
3. KEISEI ELECTRIC RAILWAY	234.4
4. DORDTSCH PETROLEUM	207.9
5. SMITHKLINE BEECHAM	150.5
6. RALSTON PURINA	66.2
7. ELSEVIER	66.0
8. RACAL TELECOMMUNICATIONS	55.0
9. SYNTEX	53.8
10. FREEPORT McMORAN	52.4
11. CANAL PLUS	51.0
12. POLYGRAM	50.6
13. GENERAL MILLS	50.0
14. FREEPORT McMORAN C&G	48.4
15. MERCK	48.2

DATA: MORGAN STANLEY CAPITAL INTERNATIONAL INC., BW

The Global 1000

were perhaps the most dramatic. The new mood in Tokyo favoring value and quality took the air out of the highfliers and shifted the focus to smaller fry. Daifuku Co., for example, an automation equipment maker, charged out of nowhere with a 35% share-price gain to land on the list for the first time. With unswerving attention to its balance sheet and its booming domestic customers, Daifuku boasted strong earnings growth and sound financials—just what investors wanted. Sales were \$847 million for the fiscal year ended in March, and earnings per share leaped by 62%.

What's even more attractive about Daifuku is that it's a growing presence in

automation, which is destined for high growth in labor-starved Japan. It could also reap big benefits as Japan's notoriously overmanned distribution system is streamlined. Daifuku is the inventor of the vertical automated warehouse, which uses computer-guided machines and huge, cage-like structures to store and retrieve parts within a factory's walls. Key to Daifuku's success, with 60% market share, is that it reduces engineering costs and delivery times by standardizing parts and design across a broad range of systems. Most competitors still engineer their products one at a time.

Daifuku's domestic orientation is typical

of the other outstanding Japanese performers. Japan's economy grew faster than the country's traditional export markets for most of the year. Top gainer Nihon Unisys Ltd., a joint venture of trading Mitsui & Co. and computer maker Unisys Corp., does all of its business in Japan. But while sales grew by a respectable 13.5%, profits plunged by 38.7%, hit by higher interest and R&D costs plus intensified competition. Analysts ascribe the company's share-price jump to takeover speculation.

More representative is Toyo Seikan Kaisha Ltd., whose 29% share-price gain was fourth-highest among Japanese companies in the Global 1000. As Japan's largest sup-

DRUGMAKERS: PRESCRIBING FOR THE HANGOVER TO COME

Just for amusement, staffers at drug industry powerhouse Merck & Co. sometimes kick back and play the Drug Research Uncertainty Game. In the computer simulation devised by Merck's financial wizards, players develop drugs and decide how much money to funnel into research. If they spend enough and are blessed with a few breakthroughs, balloons and confetti pop onto the screen. But make a bad choice or suffer lousy luck, and Devour Inc. marches over to snap up sad-faced Drugs-R-Us.

Lately there has been more champagne than chagrin for Merck and most of the world's major drug corporations. The industry has been an astounding money machine. Profits last year for 31 U.S. drugmakers combined soared 34%, while recession-hit earnings for all industries fell 4%. More impressive, generous margins allowed the drugmakers to clock the gains while boosting sales only 18%. And worldwide, the group was one of the best-performing of this year's Global 1000 in 1990 (table).

Britain's Glaxo Holdings Ltd. more than doubled its market value, as did SmithKline Beecham Corp., the newly merged drugmaker based in Britain. But the big winners this year were the Americans, who justly claim bragging rights to most of the breakthrough medicines of the previous 20 years. Merck glided into the No. 15 spot in the ranking of the world's most valuable companies, from 18th last year. Pfizer Inc. was one of the world's top gainers,

adding 79% to its market value.

But like a real-life uncertainty game, the glittering performance of the past year could tarnish a bit in the next five years. For one thing, some drugmakers have been fattening their profit margins by simply charging high prices. As the health care crisis in the U.S. and elsewhere deepens and policymakers and big buyers of drugs look for ways to rein in costs, the party could come to

Leschly, chairman of the ethical unit of SmithKline Beecham: "The game is much more difficult. It's about staying power."

LAB GRABS. Already, profit growth is slowing. At Glaxo, for instance, profits grew only 13.3% last year, a cry from the increases of more than 50% clocked only a few years ago. Likewise, the latest profit-growth rate for U.S.-based Bristol-Myers Squibb and Merck pale next to the sharp gains they logged in the 1980s.

That's one reason the industry's leaders are worried about productivity in their labs. Analyst Hemant Shah figures only some of the industry's revenues in the U.S. now come from drugs introduced in the past 10 years. The problem: Big-name areas such as cardiovascular medicine are glutted with "me too" drugs, while in areas of greatest need, opportunity, the science remains murky, and it means more spending on research to sleuth out the novel medicines.

Treating central-nervous system disorders, for

instance, is difficult and expensive. Warner-Lambert Co. has been unable to win Food & Drug Administration approval for a much-anticipated Alzheimer's disease drug, Cognex, because experts question whether the drug's dubious effectiveness justifies some of its side effects. And Eli Lilly & Co.'s blockbuster antidepressant Prozac has been blamed for causing users to commit violent crimes. The company says no connection proves the connection.

THE WORLD'S TOP DRUGMAKERS ARE FEELING NO PAIN

	Market value Billions	Share-price gain Percent change from 1990	Country
1. MERCK	\$46.0	44%	U.S.
2. BRISTOL-MYERS SQUIBB	42.4	32	U.S.
3. JOHNSON & JOHNSON	30.2	42	U.S.
4. GLAXO HOLDINGS	30.0	52	Britain
5. ABBOTT LABORATORIES	22.7	37	U.S.
6. ELI LILLY	21.2	2	U.S.
7. PFIZER	19.5	79	U.S.
8. AMERICAN HOME PRODUCTS	18.7	12	U.S.
9. SMITHKLINE BEECHAM	17.1	53	Britain
10. ROCHE HOLDING	15.3	-4	Switzerland

SOURCE: MORGAN STANLEY CAPITAL MARKETS (GLOBAL INC.)

an end. The drug companies "are obvious targets for regulatory action," says Daniel J. Duane, managing director of Prudential Securities Inc.'s global fund.

More disturbing, few blockbusters are coming down the pike to power growth the way such \$1 billion annual sellers as Merck's antihypertensive Vasotec and Glaxo's ulcer fighter Zantac have. Finally, a squeeze is on for efficiency, driven partly by a consolidation wave sweeping the industry. Warns Jan

of beverage and food cans, all of Toyo Kan's business is domestic. Booming sales, especially of Super Dry from Asahi Breweries Ltd., to which it is the main supplier, kept the coffers full. It also benefited from a shortage of canning capacity, which enabled it to extract high margins from customers.

ECOM TORTOISE. Not to be overlooked is the phenomenal performance of game maker Sega Enterprises' stock, which rose by an adjusted 161%. It failed to make this year's Global 1000 because it was listed on the Tokyo Stock Exchange in the year. Like last year's top Japanese share-price gainer, Nintendo Co., Sega is cashing in on the worldwide craze for electronic games and this year beat

Nintendo to the market with a new generation of products.

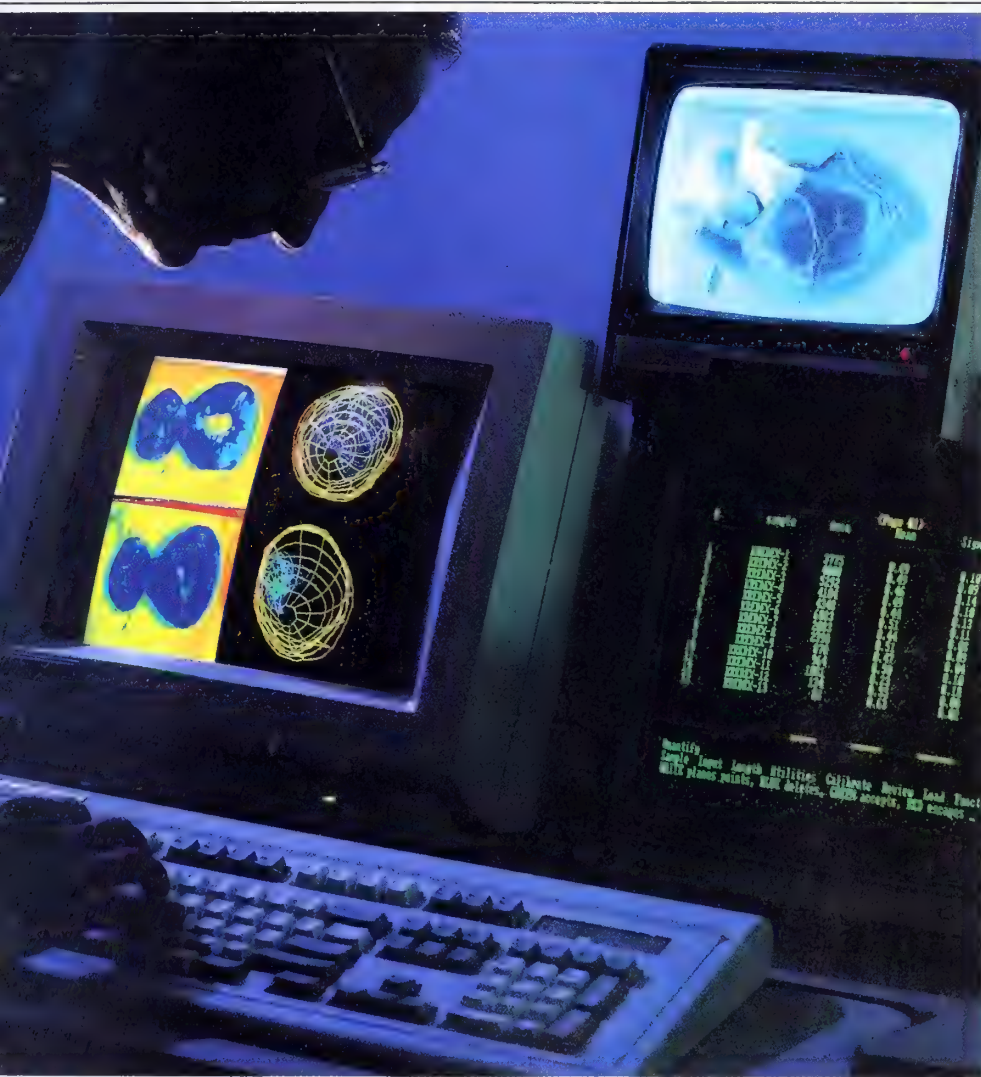
Conspicuous by its lackluster share price is NTT Corp. Down by 13% in dollar terms, the telecommunications giant's stock fell by 21% in yen. Though it beat the overall market's performance, investors remain concerned about short-term earnings and NTT's sluggishness in converting itself from a lumbering monopoly into an agile marketer. But analysts expect gains when it spins off two key subsidiaries in a few years.

To be sure, slumping stock prices are bound to blunt Japanese corporate competitiveness some. Lower price-earnings ratios and higher interest rates push up the low cost of capital, once Japan's ace in the hole.

Now Japanese companies may not invest as aggressively in capital expansion, which grew by about 15% last year and is still rising by 7% to 8%. And more debt will be coming due as bondholders cash in more often.

Even so, the rest of the world shouldn't celebrate Japan's market woes. Predicts Peter Tasker, general manager for research at Kleinwort Benson International Inc. in Tokyo: "Companies competing against the Japanese won't notice the difference." And if companies and their investors keep stressing the bottom line, Japan's strength can only improve.

By Robert Neff in Tokyo, with Blanca Riemer in Paris, Elizabeth Weiner in New York, and bureau reports



A CLOG IN THE R&D PIPELINE: ONLY SOME 15% OF DRUG REVENUES IN THE U.S. COME FROM PRODUCTS INTRODUCED IN THE LAST FIVE YEARS

can they give short shrift to marketing while building up labs.

Still, mergers and size alone won't guarantee success. The onetime darling of the industry, SmithKline, ranked No. 6 in the world when its star drug, Tagamet, lost sales badly to Glaxo's cleverly marketed Zantac in the mid-1980s. Then, when generics tore into SmithKline's sales of the blood-pressure medicine Dyzide, the company merged in 1989 into Beecham, the British over-the-counter drugmaker.

After hundreds of millions of dollars in R&D spending, the London-based company just couldn't deliver the blockbuster it needed. Even now, while it basks in gains from merger-related savings, SmithKline Beecham remains on the prowl for big new drugs. Eminase, its new heart-attack treatment, is struggling against better-known or cheaper drugs. What's more, SB is having

trouble coming up with an effective over-the-counter version of Tagamet, whose patent expires in 1994. So even while U.S. and British drugmakers seem to be enjoying their glory days, Devour Inc. is always waiting in the wings.

ers such as Yamanouchi Pharmaceutical Co. and Sankyo have gone global by licensing drugs to Merck and Bristol-Myers Squibb. The tack now is to lock up promising compounds fast and then move the drugs through government approvals simultaneously around the world. Companies can no longer afford to keep a strictly domestic focus, nor

By Joseph Weber in Philadelphia, with Mark Maremont in London

The Global 1000 — The Leaders

RANK				MARKET VALUE	RANK			MARKET VALUE	
1991	1990				1991	1990			
		Billions of U. S. dollars				Billions of U. S. dollars			
1	1	NIPPON TELEGRAPH & TELEPHONE	Japan	103.00	51	33	ATLANTIC RICHFIELD	U.S.	19.66
2	4	ROYAL DUTCH/SHELL GROUP	Neth./Britain	72.91	52	46	SIEMENS	Germany	19.61
3	6	EXXON	U.S.	72.81	53	136	PFIZER	U.S.	19.47
4	5	GENERAL ELECTRIC	U.S.	67.45	54	77	AMERICAN INTERNATIONAL GROUP	U.S.	19.20
5	3	INDUSTRIAL BANK OF JAPAN	Japan	64.18	55	79	AMERICAN HOME PRODUCTS	U.S.	18.66
6	16	PHILIP MORRIS	U.S.	63.33	56	49	BELL ATLANTIC	U.S.	18.54
7	2	INTERNATIONAL BUSINESS MACHINES	U.S.	60.77	57	84	BRITISH GAS	Britain	18.49
8	8	FUJI BANK	Japan	58.68	58	64	MITSUBISHI TRUST & BANKING	Japan	18.48
9	12	MITSUBISHI BANK	Japan	58.08	59	39	MITSUBISHI HEAVY INDUSTRIES	Japan	18.21
10	11	DAI-ICHI KANGYO BANK	Japan	57.38	60	40	TOSHIBA	Japan	18.20
11	7	SUMITOMO BANK	Japan	56.39	61	55	HANSON TRUST	Britain	18.05
12	14	SANWA BANK	Japan	49.94	62	66	B. A. T. INDUSTRIES	Britain	17.78
13	10	MITSUI TAIYO KOBE BANK	Japan	48.69	63	43	FORD MOTOR	U.S.	17.45
14	22	WAL-MART STORES	U.S.	48.55	64	60	DEUTSCHE BANK	Germany	17.36
15	18	MERCK	U.S.	46.01	65	121	SMITHKLINE BEECHAM	Britain	17.09
16	9	TOYOTA MOTOR	Japan	44.01	66	59	BOEING	U.S.	16.79
17	21	BRISTOL-MYERS SQUIBB	U.S.	42.45	67	50	NEC	Japan	16.70
18	13	AMERICAN TELEPHONE & TELEGRAPH	U.S.	40.43	68	82	TEXACO	U.S.	16.65
19	27	BRITISH TELECOMMUNICATIONS	Britain	40.03	69	62	ASSICURAZIONI GENERALI	Italy	16.57
20	23	COCA-COLA	U.S.	38.26	70	58	PACIFIC TELESIS	U.S.	16.29
21	15	TOKYO ELECTRIC POWER	Japan	37.53	71	73	AMERITECH	U.S.	15.96
22	29	DU PONT	U.S.	33.16	72	67	CHUBU ELECTRIC POWER	Japan	15.81
23	19	NOMURA SECURITIES	Japan	30.80	73	93	IMPERIAL CHEMICAL INDUSTRIES	Britain	15.67
24	25	BRITISH PETROLEUM	Britain	30.61	74	99	ELF AQUITAINE	France	15.59
25	47	JOHNSON & JOHNSON	U.S.	30.18	75	70	SUMITOMO TRUST & BANKING	Japan	15.57
26	53	GLAXO HOLDINGS	Britain	30.02	76	69	SOUTHWESTERN BELL	U.S.	15.52
27	20	LONG-TERM CREDIT BANK OF JAPAN	Japan	29.79	77	61	SONY	Japan	15.44
28	32	PROCTER & GAMBLE	U.S.	29.49	78	74	WALT DISNEY	U.S.	15.29
29	17	HITACHI LTD.	Japan	27.73	79	98	SCHLUMBERGER	U.S.	15.27
30	34	MOBIL	U.S.	26.42	80	94	ROCHE HOLDING	Switzerland	15.25
31	26	GENERAL MOTORS	U.S.	26.40	81	81	TOKIO MARINE & FIRE	Japan	15.10
32	30	AMOCO	U.S.	26.16	82	115	ANHEUSER-BUSCH	U.S.	15.08
33	35	ALLIANZ HOLDING	Germany	26.15	83	75	DOW CHEMICAL	U.S.	14.98
34	38	TOKAI BANK	Japan	26.10	84	71	FUJITSU	Japan	14.82
35	36	CHEVRON	U.S.	25.91	85	127	GUINNESS	Britain	14.72
36	48	GTE	U.S.	25.91	86	89	NINTENDO	Japan	14.56
37	24	MATSUSHITA ELECTRIC INDUSTRIAL	Japan	25.46	87	97	US WEST	U.S.	14.46
38	54	PEPSICO	U.S.	24.89	88	85	ALL NIPPON AIRWAYS	Japan	14.41
39	44	UNILEVER	Neth./Britain	24.07	89	72	NYNEX	U.S.	14.38
40	31	BELLSOUTH	U.S.	24.04	90	139	SEVEN-ELEVEN JAPAN	Japan	14.38
41	28	NIPPON STEEL	Japan	23.19	91	149	BROKEN HILL PROPRIETARY	Australia	14.27
42	78	ABBOTT LABORATORIES	U.S.	22.73	92	76	MITSUBISHI CORP.	Japan	14.26
43	41	NESTLE	Switzerland	22.03	93	52	JAPAN AIR LINES	Japan	14.23
44	137	KYOWA SAITAMA BANK	Japan	21.83	94	101	YASUDA TRUST & BANKING	Japan	14.13
45	45	ELI LILLY	U.S.	21.24	95	113	SEARS, ROEBUCK	U.S.	13.94
46	65	MINNESOTA MINING & MFG.	U.S.	20.92	96	90	DAIWA BANK	Japan	13.91
47	37	KANSAI ELECTRIC POWER	Japan	20.62	97	103	EASTMAN KODAK	U.S.	13.76
48	42	DAIMLER-BENZ	Germany	20.52	98	51	NISSAN MOTOR	Japan	13.60
49	57	BANK OF TOKYO	Japan	20.46	99	104	MITSUI TRUST & BANKING	Japan	13.53
50	63	WASTE MANAGEMENT	U.S.	19.97	100	56	NIPPON CREDIT BANK	Japan	13.44

THE BUSINESS WEEK GLOBAL 1000

COUNTRY BY COUNTRY

SUMMARY

MARKET VALUE:

Market price on May 31, 1991, multiplied by the available number of shares outstanding, translated into U. S. dollars at May month-end exchange rates. Market value may include all classes of stock; price and yield data based on the company's most widely held shares.

PERCENTAGE PRICE AND ANNUAL CHANGE:

Percent change in share price on May 31, 1991, in U. S. dollars. Annual percent change from May 31, 1990, to May 31, 1991, both in U. S. dollars and in each company's local currency.

PRICE/BOOK VALUE RATIO:

The ratio of May closing price to latest available net worth per share or common shareholders' equity investment.

PRICE/EARNINGS RATIO:

The ratio of May closing price to latest 12 months' earnings per share.

YIELD:

Latest 12 months' dividends per share as a percent of May closing price.

SALES:

Net sales reported by company, translated at May 31 exchange rates; revenues for banks and other financial institutions are not included because they are not comparable to those of industrial companies.

PROFITS:

Latest aftertax earnings available to common shareholders, translated at May 31 currency exchange rates; profits are from companies' continuing operations before extraordinary items. Sales, profits, and assets are for 1990 fiscal year unless noted.

RETURN ON EQUITY:

Latest 12-months' earnings per share as percent of most recent book value per share.

INDUSTRY CODE:

For key to the two-digit code, see page 103.

Data for individual companies: Morgan Stanley Capital International, unless otherwise indicated. Country composites and rankings calculated by BUSINESS WEEK. Additional data by Standard & Poor's Compustat Services Inc. if footnoted.

	GLOBAL 1000 RANK	MARKET VALUE U. S. \$ MIL.	PRICE PER SHARE U. S. \$	% CHANGE FROM 1990 (U. S. \$) (LOCAL)		PRICE/ BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U. S. \$ MIL.	PROFITS U. S. \$ MIL.	ASSETS U. S. \$ MIL.	RETURN ON EQUITY %	INDUSTRY CODE
GLOBAL POSITIVE	6722269	191	-1	-4	2.8	23	3.2	7211182	334331	21475646	15.1		
AUSTRALIA													
COUNTRY COMPOSITE	63967	6	8	9	1.8	14	5.1	57806	5017	286504	13.4		
Broken Hill Proprietary	91	14274	9	32	34	2.4	15	3.3	10209	839	16445	16.6	11
National Australia Bank	300	5904	5	4	6	1.1	11	7.6	NA	583	71957	9.5	61
CRA	321	5631	10	2	4	1.8	18	3.5	3494	307	5961	9.6	24
BTR Nylex	355	5179	2	0	1	2.6	13	4.0	3679	399	4697	19.9	37
Coles Myer	421	4439	8	46	47	2.6	16	3.4	11197	278	3978	16.3	54
Westpac Banking	448	4245	4	-5	-4	0.8	7	8.9	NA	520	81389	10.8	61
Western Mining	574	3359	4	3	5	1.6	10	6.2	1050	327	3009	16.3	24
CSR	580	3319	4	6	7	1.6	11	7.1	3435	310	4792	14.5	71
Pacific Dunlop Olympic	654	2946	4	9	10	3.0	13	3.9	3840	229	3234	22.6	71
ANZ Group Holdings	700	2749	3	-30	-29	0.8	9	7.2	NA	314	75106	9.3	61
Brambles Industries	744	2610	13	24	25	2.7	16	2.9	1565	161	1862	16.3	52
Fosters Brewing Group	747	2600	1	-19	-18	1.3	24	1.6	11708	245	6411	5.2	59
Boral	811	2386	3	-2	-1	1.5	12	7.1	3009	245	3078	13.2	21
Lend Lease	815	2369	12	26	27	2.0	17	3.8	1293	122	1625	12.3	64
Amcor	986	1957	4	23	25	1.5	16	5.1	3326	138	2958	9.0	23
AUSTRIA													
COUNTRY COMPOSITE	7344	283	-5	-3	5.6	58	1.1	891	189	72007	10.9		
Creditanstalt-Bankverein	656	2928	383	-21	-20	1.7	61	1.6	NA	52	46722	2.7	61
EA-Generali	817	2364	364	5	7	11.2	90	0.4	891a	26a	1756a	12.4	63
Oesterreichische Landesbank	947	2051	103	1	3	4.0	23	1.1	NA	111	23529	17.6	61
BELGIUM													
COUNTRY COMPOSITE	34629	181	-6	-4	1.8	13	5.1	35439	2661	133453	13.6		
Petrofina	239	7330	330	-4	-2	2.0	12	4.8	16282	597	10741	16.5	11
Electrabel	270	6494	127	10	12	1.5	11	8.2	2242a	219a	4853a	13.8	12
Société Générale de Belgique	507	3832	65	-31	-30	1.0	11	4.9	NA	344	15648a	8.7	71
Tractebel	594	3254	237	-6	-4	1.4	14	4.8	944a	220	4255a	10.0	71
Solvay	614	3145	380	-8	-6	1.3	7	4.9	7183	459	6859a	18.9	22
Delhaize-Le Lion	861	2235	218	21	23	5.6	21	1.2	7493	105	2084	26.5	54
Electrafina	872	2197	87	-7	-5	1.1	12	5.3	NA	167	2159a	9.5	11
Groupe Bruxelles Lambert	906	2128	103	-11	-9	1.4	9	5.4	NA	247	3958a	16.2	71
Générale de Banque	938	2063	144	0	2	0.9	9	7.1	NA	226	68620a	10.2	61
Royale Belge	990	1951	123	-25	-24	1.5	25	4.0	1296a	77	14276a	5.8	63

Based on nonconsolidated results. ** Based on nonconsolidated earnings per share and consolidated book value per share. a) Based on 1989 data. b) Based on 1991 data. c) Partial year data of fiscal-year change. 1) Global ranking calculated for Royal Dutch/Shell Group combining market value of the Netherlands' Royal Dutch Petroleum and Britain's Shell Transport & Trading. 2) Global ranking calculated for Unilever by combining market value of the Netherlands' Unilever NV and Britain's Unilever PLC. 3) Global ranking calculated for Eurotunnel by combining market of Eurotunnel (London) and Eurotunnel (Paris). Sales, profits, and assets in the individual country listings are for the three combined companies above; share price and relative ratios are for the companies. 4) Global ranking calculated for ABB Asea Brown Boveri by combining market value of Sweden's ASEA and Switzerland's BBC Brown Boveri. 5) Data for this company provided by Standard & Poor's Compustat Services Inc. Unless otherwise noted, all other data provided by Morgan Stanley Capital International. LOSS = Negative ratio. NA = Not available. NEG = Negative return. NM = Not meaningful. NR = Not ranked.

THE GLOBAL 1000

COUNTRY RANK		GLOBAL 1000 RANK	MARKET VALUE U. S. \$ MIL.	PRICE PER SHARE U. S. \$	% CHANGE FROM 1990 (U. S. \$) (LOCAL)		PRICE/BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U. S. \$ MIL.	PROFITS U. S. \$ MIL.	ASSETS U. S. \$ MIL.	RETURN ON EQUITY %	INDU CO.
BRITAIN														
COUNTRY COMPOSITE		614915		7	6	5	2.9	14	5.1	680206	48540	1617205	20.2	
1	British Telecommunications	19	40035	7	35	33	2.5	11	4.9	22500b	3559b	32749	22.3	5
2	British Petroleum	24	30610	6	3	1	1.6	13	6.5	56463	2874	52528	12.2	1
3	Glaxo Holdings	26	30022	20	52	49	7.6	21	2.7	4883	1357	7469	36.0	4
4	Shell Transport & Trading (1)	NR	28923	9	11	9	1.5	13	5.3	106479	6533	106431	11.9	1
5	British Gas	57	18490	4	19	17	1.5	11	6.6	13659	1584	20707	12.8	1
6	Hanson Trust	61	18045	4	-7	-8	3.7	11	5.5	12242	1661	25244	35.2	7
7	B. A. T. Industries	62	17782	12	10	8	3.6	27	6.0	13765	607	42722	13.4	4
8	SmithKline Beecham	65	17092	14	53	50	28.6	19	2.5	7701	931	6654	150.5	4
9	Imperial Chemical Industries	73	15673	22	10	8	2.0	19	5.7	22082	1056	18477	10.2	2
10	Guinness	85	14722	16	27	24	2.5	15	2.6	4300	926	11267	16.9	4
11	Grand Metropolitan	104	13131	13	28	26	2.6	13	3.7	16073	1085	16118	20.4	7
12	Barclays Bank	111	12067	8	13	11	1.2	18	6.4	NA	669	230815	6.4	6
13	Marks & Spencer	118	11532	4	14	12	3.1	16	3.6	9873b	683b	5908	18.7	5
14	BTR	119	11498	7	-7	-9	4.2	12	5.4	11536	946	9905	34.6	7
15	Unilever PLC (2)	NR	10548	13	14	12	5.0	13	3.2	39620	1980	14139	38.5	4
16	J. Sainsbury	150	10041	6	29	27	4.0	16	2.6	14030b	537	5739	25.0	5
17	Tesco	168	9383	5	29	27	2.5	15	2.5	11515b	518b	6286b	16.4	5
18	Cable & Wireless	171	9316	9	-5	-7	2.5	16	2.8	3963	561	7481	15.5	5
19	General Electric	179	9003	3	-5	-7	2.3	10	6.8	15033	929	10182	22.4	3
20	RTZ	185	8819	9	-7	-8	2.0	10	5.0	8689	867	10093	19.9	2
21	National Westminster Bank	187	8801	5	-8	-10	0.9	24	7.3	NA	354	207203	3.6	6
22	Wellcome	200	8467	10	-10	-12	5.7	26	1.8	2513	330	2582	22.2	4
23	Allied-Lyons	213	8026	9	17	15	1.7	11	4.3	7068	618	10281	14.8	4
24	Prudential	233	7452	4	8	6	8.7	39	5.9	8880	190	62537	22.2	6
25	Lloyds Bank	235	7427	6	23	20	1.9	15	5.8	NA	500	94448	13.1	6
26	Bass	242	7238	17	-5	-7	1.2	10	4.5	6440	804	9907	11.9	4
27	Racal Telecommunications	267	6588	7	4	2	14.3	26	1.5	695	202	777	55.0	5
28	Abbey National	273	6325	5	41	39	NA	10	4.5	NA	638	NA	NA	61
29	Boots	274	6304	6	31	29	3.2	15	4.0	5785	419	4177	21.7	5
30	Reuters Holdings	278	6257	14	-28	-30	6.6	17	2.4	2342	354	1679	39.0	5
31	Fisons	309	5721	8	35	33	8.0	18	2.1	2062	306	1982	43.5	4
32	Argyll Group	330	5576	5	31	29	3.0	14	3.9	8144b	358b	2946	22.1	5
33	Great Universal Stores	348	5235	21	22	19	1.1	11	3.7	4608	467	6278	9.9	5
34	Racal Electronics	362	5106	4	12	10	3.9	24	2.1	3378	200	3372	15.8	7
35	Sun Alliance & London Insurance	372	4974	6	17	15	1.4	LOSS	5.2	5773	-181	10988	NEG	6
36	Rothmans International	390	4775	15	30	27	3.1	13	2.4	2650	347	3903	23.9	4
37	Lloyds Abbey Life	406	4634	7	24	21	2.8	13	5.8	1773	359	8413	22.2	6
38	Land Securities	424	4410	9	3	1	0.6	17	5.1	NA	267b	10271	3.5	6
39	BOC Group	432	4355	9	-1	-3	2.2	11	4.9	4524	414	4825	19.7	2
40	British Steel	435	4347	2	-10	-11	0.7	5	8.9	8743	965	9450a	12.0	2
41	Cadbury Schweppes	437	4337	6	8	6	3.3	14	4.3	5383	301	4041	23.0	4
42	Associated British Foods	471	4063	9	35	32	1.2	11	3.1	5347b	359b	4254	10.9	4
43	Peninsular & Oriental Steam Navigation	475	4033	10	-7	-9	1.5	13	7.2	8606	317	8256	11.0	5
44	General Accident Fire & Life Assurance	478	4014	9	0	-2	1.6	LOSS	6.6	5918	-159	15757	NEG	6
45	Enterprise Oil	485	3964	9	-22	-23	3.6	15	3.9	850	269	3328	24.7	1
46	Reckitt & Colman	497	3874	26	22	20	5.3	15	3.0	3018	260	2756	35.2	4
47	Whitbread	498	3873	9	21	19	0.9	11	4.2	3850b	359b	5802	8.2	4
48	Ladbroke Group	508	3826	4	-16	-17	0.9	10	5.5	6504	392	8030	9.2	5
49	Thorn EMI	518	3756	12	-1	-3	3.3	10	5.7	6262b	342	4548	31.8	4
50	Kingfisher	519	3744	8	51	48	2.2	11	3.4	5333b	323b	3412b	19.6	5
51	Reed International	520	3741	7	-8	-10	1.6	11	4.9	2700	361	4551	14.3	5
52	BAA	531	3688	7	5	3	5.4	26	3.8	1278	448	4803	20.8	5
53	Rank Organisation	532	3676	12	-13	-15	1.3	10	5.9	2281	318	5621	12.6	5
54	Commercial Union Assurance	535	3652	8	4	2	1.7	NM	6.2	6153	2	26931	0.1	6
55	Royal Insurance Holdings	537	3647	7	-6	-7	0.8	LOSS	8.4	6177	-299	17084a	NEG	6
56	Trusthouse Forte	544	3612	5	-2	-4	0.7	14	4.9	4519b	253b	7891b	5.0	5
57	TSB Group	549	3537	2	-9	-10	1.1	10	6.5	NA	330	43597a	11.4	6
58	Legal & General Group	551	3526	7	10	8	7.2	35	5.6	4449	99	27992	20.3	6
59	Pearson	567	3390	12	1	-1	2.8	12	4.2	2626	269	2993	22.5	7
60	Wiggins Teape Appleton	575	3357	4	15	13	1.9	11	4.6	4447	298	3578	17.2	2
61	National Power	628	3082	2	NA	NA	NA	NA	NA	NA	NA	NA	NA	12
62	Redland	632	3066	9	-4	-5	1.7	11	6.2	2738	246	3475	15.9	2
63	Guardian Royal Exchange	647	2980	3	-14	-16	1.8	LOSS	7.9	3487	-253	8391	NEG	6
64	Tarmac	658	2918	4	-12	-13	1.1	13	6.7	6324	210	5383	8.4	2
65	Midland Bank	669	2886	4	-23	-24	0.7	LOSS	5.6	NA	-330	102045	NEG	6
66	United Biscuits (Holdings)	687	2816	6	6	4	2.8	12	5.3	4661	224	2605	23.0	4
67	Courtaulds	699	2756	7	21	19	NA	11	3.8	3258	216	NA	NA	22
68	Scottish & Newcastle Breweries	710	2693	7	23	21	1.3	12	4.6	2122	190	3687	10.8	4
69	MEPC	714	2687	8	-1	-3	0.5	16	5.2	NA	178	7544a	3.4	6
70	Lorrho	730	2647	4	-3	-5	1.1	10	8.8	5383	253	6374	10.9	7
71	British Aerospace	739	2631	10	12	10	0.6	6	5.6	18034	409	15897	9.7	3
72	Rolls Royce	756	2565	3	-29	-30	1.3	11	6.2	6279	229	4871	11.5	3
73	Royal Bank of Scotland Group	791	2447	3	5	3	0.9	14	6.1	NA	272	51501	6.6	6
74	Maxwell Communication	821	2353	4	7	5	1.4	11	9.8	2125	217	7191	12.6	5
75	ASDA Group	828	2328	2	9	7	1.3	13	5.5	6074	210	4635	9.9	5

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THE GLOBAL 1000

	GLOBAL 1000 RANK	MARKET VALUE U. S. \$ MIL.	PRICE PER SHARE U. S. \$	% CHANGE FROM 1990 (U. S. \$) (LOCAL)		PRICE/ BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U. S. \$ MIL.	PROFITS U. S. \$ MIL.	ASSETS U. S. \$ MIL.	RETURN ON EQUITY %	INDUSTRY CODE
BET	847	2278	3	-27	-28	2.6	6	9.9	4611	484	3684	39.9	71
Blue Circle Industries	855	2252	4	-1	-2	1.7	8	6.3	2079	228	3214	20.1	21
Williams Holdings	870	2201	5	0	-2	3.3	11	5.6	1940a	162a	1315a	29.8	21
RMC Group	878	2186	11	-8	-10	2.1	10	4.1	4432	228a	2778a	21.2	21
Smith & Nephew	879	2186	2	15	13	6.7	14	4.5	1249	168	1359	47.1	45
Pilkington	882	2172	3	-18	-20	1.5	8	8.5	4988	317	5169	18.4	26
Eurotunnel (London) (3)	NR	2166	8	1	-1	1.8	NM	0.0	NA	2a	3725	0.1	52
Hillsdown Holdings	892	2154	4	-9	-10	2.4	7	4.5	7220	255a	3032a	32.9	44
Sears	907	2126	1	-13	-15	0.9	8	8.6	3696b	286	3828	11.1	54
British Airways	908	2124	3	-15	-16	1.4	13	6.9	8384b	163b	6616	10.4	56
Inchcape	910	2122	6	22	19	3.0	13	4.7	5631	164	2774	23.5	59
BICC	937	2067	7	1	-1	3.1	11	5.9	6656	178	3282a	28.5	37
Bank of Scotland	944	2055	2	14	12	1.2	14	5.1	NA	123b	33382b	8.6	61
Trafalgar House	950	2045	4	-26	-27	1.5	20	10.3	5908	188	4288	7.4	71
Thames Water	965	2012	5	47	44	1.2	9	3.1	1047	287	3082	14.4	52
Asmo	981	1970	5	-26	-27	1.3	15	3.5	613	130	3431	8.8	11
PowerGen	983	1968	3	NA	NA	NA	NA	NA	NA	NA	NA	NA	12
Cate & Lyle	984	1965	6	16	14	2.3	9	3.9	5783	198	3108	23.9	44
Willis Corroon	988	1955	5	1	-1	5.4	15	6.2	NA	89	3384	36.0	63

ADA

TRY COMPOSITE		119281	27	7	5	1.7	27	3.5	98264	9006	587139	10.0	
BCE (Bell Canada Enterprises)	123	11332	37	10	7	1.3	12	6.0	16050	1002	36680	10.8	55
Seagram	145	10268	109	27	24	1.7	14	1.8	6127b	756b	11477b	12.6	43
Northern Telecom	176	9126	37	35	32	2.8	20	0.9	6769	460	6842	14.1	34
Imperial Oil	177	9045	47	-4	-6	1.4	21	3.3	9869	456	13278	6.7	11
Thomson	214	7930	14	15	12	2.6	24	3.1	5364	420	6955a	10.8	51
Royal Bank of Canada	262	6687	22	11	9	1.4	9	4.6	NA	843	109980	15.1	61
Canadian Pacific	316	5670	18	-5	-7	0.8	24	4.5	9172	310	17663	3.5	71
Canadian Imperial Bank of Commerce	360	5120	28	21	18	1.2	8	4.1	NA	701	99760	14.3	61
Toronto-Dominion Bank	383	4866	16	5	3	1.3	12	4.1	NA	521	58441	11.3	61
Alcan Aluminium	392	4746	21	-6	-8	1.0	14	5.3	8757	543	10649	7.0	24
Shell Canada	484	3965	35	9	6	1.4	21	2.2	4812	273	5384	6.5	11
Bank of Montreal	521	3729	32	39	36	1.2	9	5.8	NA	456	76322	14.1	61
Inco	536	3649	35	27	24	0.9	12	2.9	3108	329	4058	7.6	24
Inasco	579	3344	28	-10	-12	1.6	15	4.0	3049	254	4756	10.6	43
Noranda	582	3305	17	4	1	1.0	LOSS	5.0	8356	105	13031	NEG	24
PanCanadian Petroleum	589	3273	26	8	5	2.3	17	2.0	832	185	2532	13.5	11
Placer Dome	618	3125	13	-18	-20	1.7	66	2.0	943	64	2698	2.7	81
Bank of Nova Scotia	630	3072	16	31	28	1.1	8	5.6	NA	447	76191	14.3	61
American Barrick Resources	683	2838	21	12	9	5.1	45	0.5	252	58	1050a	11.2	81
Moore	704	2735	28	-2	-4	1.8	21	3.3	2770	155	2166	8.5	52
Laidlaw	708	2725	11	-52	-53	1.6	13	2.6	1518	231	3402	12.0	57
TransCanada PipeLines	800	2413	16	19	16	2.2	14	4.0	2649	188	4577	14.9	12
Nova Corp. of Alberta	808	2391	8	12	9	1.2	17	5.7	4137	162	6128	7.2	12
Trizec	975	1982	14	-21	-23	1.8	LOSS	2.3	1107	43	9993	NEG	64
MacMillan Bloedel	993	1944	19	22	19	1.5	197	2.8	2623	45	3122	0.8	23

MARK

TRY COMPOSITE		15793	5983	5	7	6.4	69	1.8	2802	249	111310	10.3	
Dampskibsselskabet Af 1912	612	3148	14576	-9	-6	17.3	152	0.4	NA	21a	244a	11.4	58
Dampskibsselskabet Svenborg	619	3118	20920	-10	-8	14.1	136	0.3	NA	23a	274a	10.3	58
Carlsberg	705	2734	240	15	18	3.4	28	0.9	1583	101	2023	12.3	43
Den Danske Bank	707	2726	52	0	3	0.9	LOSS	4.7	NA	-177	58757	NEG	61
Novo-Nordisk	911	2121	67	42	46	2.0	18	0.9	1218	115	1890	11.3	45
Unidanmark	992	1945	42	-11	-8	0.8	12	3.6	NA	166	48123	6.4	61

LAND

TRY COMPOSITE													
		2168	16	NA	NA	0.8	27	2.0	5709	86	8734	3.0	
Repola	883	2168	16	NA	NA	0.8	27	2.0	5709	86	8734	3.0	23

ANCE

TRY COMPOSITE	183816	151	-13	-11	2.2	17	3.4	273661	16274	1491987	15.5		
Elf Aquitaine	74	15592	64	3	6	1.2	9	4.2	29879	1815	37058	14.4	11
Alcatel Alsthom	128	11092	102	-8	-6	2.0	13	3.1	24586	878	33208	15.5	34
LVMH Moët Hennessy	149	10119	728	-11	-8	3.5	18	2.4	3386	576	7717	20.0	43
Compagnie Générale des Eaux	184	8857	454	-5	-2	3.6	23	2.3	19976	379	18443a	15.6	52
BSN	192	8612	155	2	5	2.2	16	2.1	9031	528	10125	13.7	44
Union Assurances Paris	203	8404	100	-8	-6	1.6	12	2.8	16613	720	45177a	14.0	63
Compagnie Financière de Suez	220	7771	60	-27	-25	0.9	12	3.4	NA	634	137152	7.7	61
L'Air Liquide	286	6127	120	0	2	2.6	18	2.8	4937	337	6240	14.3	22
L'Oréal	307	5745	99	5	8	3.2	19	1.8	5184	310	4292	17.2	45
Paribas	318	5643	81	-30	-28	1.1	13	3.8	NA	434	161328	8.5	61
Société Générale	354	5189	75	-30	-28	1.1	11	5.1	NA	457	191224	10.0	61
Peugeot	358	5142	103	-29	-27	0.6	3	4.0	27318	1588	19723	20.0	42
Axa	361	5106	185	-24	-22	1.4	9	2.9	NA	573	29776a	16.0	71
Compagnie de Saint-Gobain	374	4944	76	-27	-25	1.1	9	4.9	11798	574	15257	12.9	26

Do more.

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System 7 makes Macintosh computers even easier to use.

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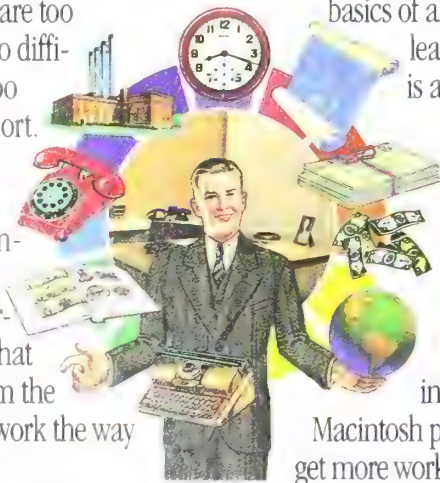
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At Apple, we couldn't agree more. We believe most PCs are too hard to set up. Too difficult to use. And too expensive to support.

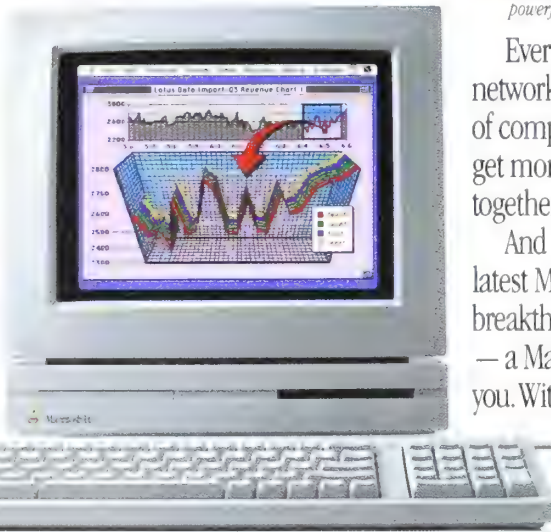
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System 7 for Macintosh. 

THE GLOBAL 1000

COUNTRY RANK		GLOBAL 1000 RANK	MARKET VALUE U.S. \$ MIL.	PRICE PER SHARE U.S. \$	% CHANGE FROM 1990 (U.S. \$) (LOCAL)		PRICE/BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL.	PROFITS U.S. \$ MIL.	ASSETS U.S. \$ MIL.	RETURN ON EQUITY %	INDUS. CODE
15	Total Francaise Pétroles	378	4894	134	7	10	0.9	7	4.4	21854	693	18078	12.6	1
16	Lyonnaise des Eaux-Dumex	401	4682	102	-21	-19	2.5	19	2.5	12068	243	16237	13.1	7
17	Carrefour	433	4355	341	6	9	3.7	19	2.4	12950	231	5284	19.7	5
18	Euro Disney	554	3515	21	9	12	3.0	NA	0.0	639*	65	1526*	NA	5
19	Lafarge Coppee	555	3496	65	-24	-22	1.8	9	3.5	5556	374	7856	19.0	2
20	Rhone-Poulenc	566	3400	60	-25	-23	1.0	127	6.7	13456	187	18636	0.8	2
21	Canal Plus	573	3359	183	12	15	11.0	22	2.5	1047	155	2061	51.0	5
22	Havas	595	3241	84	-29	-27	3.5	17	2.1	4040	188	2984	20.5	5
23	Compagnie de Navigation Mixte	638	3041	225	-28	-26	1.5	4	4.5	NA	774a	7811a	39.0	7
24	Pechiney	657	2925	58	-2	1	1.0	8	6.6	13130	381	12397	13.2	2
25	Thomson-CSF	661	2909	26	17	20	1.0	8	6.7	6321	371	12080	12.6	3
26	Groupe Victoire	664	2904	171	-29	-27	1.6	9	2.3	NA	313	32576a	16.9	6
27	Crédit Lyonnais	668	2888	99	-35	-33	0.5	5	6.0	NA	633	249787	10.4	6
28	Accor	684	2834	133	-25	-23	2.0	21	2.9	3899	136	4623	9.6	5
29	BNP	693	2784	45	-43	-41	0.4	10	2.9	NA	276	253714	3.9	6
30	Sanofi	751	2589	151	-16	-14	1.5	18	3.7	3168	146	3505	8.7	4
31	Pechelbronn	794	2433	216	-32	-30	1.6	12	2.1	NA	201	1815	13.1	7
32	Pernod Ricard	810	2387	203	-11	-8	2.2	12	3.8	2875	191	3067	17.9	4
33	Perrier	845	2285	254	-15	-12	6.4	39	2.3	2629	59	2438a	16.5	43
34	Pechiney International	859	2248	29	11	14	1.2	15	3.1	7346	155	7041	8.2	26
35	Eurotunnel (Paris) (3)	NR	2206	8	2	5	0.8	NM	0.0	NA	2a	3725	0.0	52
36	Credit Foncier de France	925	2084	217	-12	-10	3.7	17	4.3	NA	119	55592	21.4	61
37	Alcatel Cable	945	2053	622	3	6	2.8	12	3.3	4243	175	3029	23.6	37
38	Compagnie Bancaire	960	2021	97	-12	-10	1.1	12	2.6	NA	170	43025	9.5	62
39	CMB Packaging	979	1972	25	-33	-31	1.2	16	3.7	4169	125	4239	7.4	26
40	Cap Gemini Sogeti	980	1970	63	-25	-23	3.5	16	2.9	1566	106	2140	21.4	52

GERMANY

COUNTRY COMPOSITE		248609	403	-11	-9	3.7	27	3.3	446767	10584	1169933	13.7		
1	Allianz Holding	33	26153	1453	1	3	4.5	43	0.7	18427a	545a	77164a	10.3	63
2	Daimler-Benz	48	20525	441	-9	-7	2.2	16	2.5	49725	975	38981	13.6	42
3	Siemens	52	19611	376	-12	-10	2.1	15	3.1	36576	896	37308	14.3	34
4	Deutsche Bank	64	17360	393	-14	-12	2.0	NA	3.2	NA	618	230391	NA	61
5	Bayer	133	10864	170	-3	-1	1.3	10	6.9	24106	1089	21962	13.0	22
6	RWE	139	10394	245	-14	-12	2.7	17	3.7	25606	454	28342	15.6	12
7	Münchener Rück.	148	10238	1401	3	6	24.6	118	0.6	7324	39	19589	20.8	63
8	VEBA	154	9855	221	-13	-11	1.4	14	4.5	31778	633	23977a	10.4	12
9	Hoechst	172	9302	160	-6	-4	1.4	10	7.3	25969	867	19792	13.7	22
10	BASF	195	8578	151	-14	-12	1.1	11	7.8	26989	641	21274	10.1	22
11	Dresdner Bank	218	7798	223	-8	-6	1.5	NA	4.9	NA	365a	142923a	NA	61
12	Volkswagen	240	7325	228	-36	-34	1.0	7	4.4	39399	570a	32920a	15.7	42
13	Siemens Nixdorf Informationssysteme	289	6027	161	-21	-19	3.6	LOSS	0.0	1984c	-461	2207	NEG	33
14	BMW	350	5229	329	-6	-4	1.6	10	3.4	15716	403	13025	16.1	42
15	Mannesmann	359	5138	162	-22	-21	1.7	12	5.0	13881	268a	9389a	14.9	38
16	Henkel	373	4953	353	-2	0	2.5	19	2.4	6956	225	5304	13.4	44
17	Hochtief	425	4399	880	12	15	5.5	NA	1.0	3479	48	2519a	NA	32
18	Mercedes-Automobil-Holding	447	4246	361	-9	-7	2.8	NA	3.0	NA	74a	1291a	NA	42
19	Thyssen	480	4000	127	-25	-23	1.4	7	7.1	20947	368	13243	20.3	25
20	Commerzbank	482	3999	155	-5	-3	1.1	NA	5.8	NA	318	124689	NA	61
21	VIAG	494	3890	219	-7	-5	1.7	14	3.3	11259	144a	6902a	12.6	71
22	Bayerische Vereinsbank	529	3703	234	8	10	1.5	NA	5.0	NA	181	118958	NA	61
23	Bayerische Hypotheken	541	3621	219	-2	1	1.4	NA	5.4	NA	176	100724	NA	61
24	Linde	576	3355	491	-14	-12	2.3	20	2.8	3513	123	3349	11.7	38
25	MAN	588	3274	226	-21	-19	2.1	15	4.4	10962	180	10049	13.9	38
26	Schering	593	3260	477	6	9	2.4	20	2.5	3429	149	3689	12.0	45
27	Preussag	650	2970	210	-21	-20	2.1	8	4.6	11025c	181	7873	24.9	71
28	Karstadt	712	2692	374	-7	-5	2.9	37	2.9	9667	81a	3023a	7.8	54
29	Rheinelektra	715	2682	958	-21	-19	27.3	88	1.1	377*	25	390*	30.9	38
30	Kaufhof	721	2661	311	-17	-16	3.5	38	3.1	8452	51a	2743a	9.2	54
31	Philipp Holzmann	771	2517	895	-2	0	4.7	NA	1.0	3569a	76a	2740a	NA	32
32	Vereinigte Elektrizitätswerke Westfalen	793	2437	122	-8	-6	2.1	18	4.8	3664	88a	5945a	11.5	12
33	Isar-Amperwerke	806	2400	365	4	6	7.0	78	2.0	962	29	2001	9.0	12
34	Metallgesellschaft	814	2369	310	-16	-15	2.3	22	2.9	11477	112	6488	10.4	71
35	Aachener & Münchener Bet.	835	2304	493	-8	-6	1.6	27	2.3	NA	40a*	1405a*	6.0	63
36	Deutsche Lufthansa	850	2261	75	-26	-25	1.3	32	0.0	8365	64a	7109a	3.9	56
37	Victoria Holding	885	2165	984	-29	-27	4.6	NA	0.8	2314a	44a	13766a	NA	63
38	AEG	952	2038	109	-37	-36	2.3	NA	2.1	7583	-149	5279	NA	34
39	Heidelberger Zement	963	2014	671	-14	-12	5.5	32	1.2	1285	53a	1210a	17.3	21

HONG KONG

COUNTRY COMPOSITE		61658	2	24	23	2.4	12	4.5	24188	4728	229571	18.8		
1	Hong Kong Telecommunications	156	9803	1	20	19	7.5	17	4.9	2103b	561b	1943	43.0	55
2	Hutchison-Whampoa	293	5986	2	38	37	1.9	13	4.3	2068	455	6396	14.3	71
3	HSBC Holdings	334	5526	3	12	11	0.8	14	5.9	NA	400	149690	5.8	61
4	Cheung Kong Holdings	375	4943	2	41	40	2.0	12	2.8	570	420	2871	17.2	64
5	China Light & Power	418	4460	3	54	53	3.4	13	3.8	1369	300	2306	26.0	12
6	Sun Hung Kai Properties	454	4205	2	35	34	1.5	12	4.3	831	319	4274	12.2	64

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Hong Seng Bank	456	4148	3	60	59	2.3	15	4.4	NA	283	27844	15.5	61
Swire Pacific	510	3817	2	-4	-4	1.0	12	4.3	4033	317	8406	8.5	71
Cathay Pacific Airways	613	3147	1	-4	-4	2.4	8	4.9	2562	387	4103	30.1	56
Hongkong Electric Holdings	629	3082	2	48	48	3.3	12	5.2	560	249	1933	26.5	12
Hongkong Land Holdings	694	2781	1	-2	-3	0.7	10	7.7	NA	268	5548	6.4	64
Jardine Matheson Holdings	702	2736	4	-5	-6	1.9	12	3.4	6035	230	6592	16.7	71
Wharf (Holdings)	789	2454	1	17	17	0.7	13	5.0	403	161	4100	5.6	52
Dairy Farm International Holdings	812	2381	1	9	9	4.9	16	3.2	3654	152	1674	31.7	54
Henderson Land Development	877	2187	1	43	42	1.8	8	3.5	NA	225	1892	22.9	64

LAND

TRY COMPOSITE		1980	9	-9	-8	1.9	11	0.8	1540	183	2470	17.3		
Smurfit Group		976	1980	9	-9	-8	1.9	11	0.8	1540b	183b	2470	17.3	23

LY

TRY COMPOSITE		84156	12	-13	-10	2.7	20	2.5	105066	5463	461349	12.8	
Assicurazioni Generali	69	16575	28	-11	-9	4.5	37	1.0	8133a	449a	28184a	12.1	63
Fiat Group	153	9896	5	-46	-45	0.9	9	6.2	44702	1260	45892a	10.3	42
STET	210	8057	2	-14	-11	1.0	11	4.4	15599	742a	38856a	9.3	55
SIP	384	4850	1	-21	-19	0.5	15	5.3	13065	314	33028a	3.4	55
Alleanza Assicurazioni	413	4520	44	30	34	11.1	45	0.9	343a*	102*	5417a*	25.0	63
Mediobanca	417	4475	13	-23	-21	3.1	25	1.2	NA	180*	14218*	12.7	61
Montedison	419	4450	1	-17	-15	NA	11	3.3	11517	434	NA	NA	71
Banca Commerciale Italiana	501	3857	4	-10	-8	1.1	11	4.1	NA	373	81810	10.4	61
Credito Italiano	597	3238	2	-5	-2	1.3	13	3.1	NA	264	73507a	10.2	61
RAS	616	3138	16	-24	-22	2.6	32	1.4	3115a	110a	9705a	8.2	63
La Fondiaria	685	2833	35	-32	-30	3.7	31	1.3	1882a	91a	5497a	12.0	63
Banco di Roma	701	2746	2	10	13	1.3	22	1.7	NA	126a	64004a	6.1	61
Banco Ambrosiano Veneto	805	2400	4	-5	-2	2.0	17	2.7	NA	152	23491	11.9	61
Ferruzzi Finanziaria	822	2346	2	-29	-27	1.0	13	1.9	NA	194	24673a	8.0	71
Arnoldo Mondadori Editore	824	2335	10	-25	-23	2.2	18	1.0	1819	43	2173a	11.9	51
SAI	842	2293	16	-3	0	3.5	38	0.8	1349a	67	3790a	9.2	63
Italcementi	930	2077	18	-16	-14	1.8	15	1.4	1217	161	2073a	12.0	21
Sirti	934	2071	9	-5	-3	2.8	12	4.1	920	174	1586	23.6	32
Toro Assicurazioni	966	1998	21	3	6	3.9	11	1.1	1406	227	3444a	34.7	63

AN

TRY COMPOSITE		2346556	14	-11	-19	3.9	60	0.7	2464560	60166	7972670	8.6	
Nippon Telegraph & Telephone	1	102999	6600	-13	-21	3.6	60	0.5	45247b	1709b	82683	5.9	55
Industrial Bank of Japan	5	64179	27	-5	-14	7.4	134	0.2	NA	478b	325809	5.5	61
Fuji Bank	8	58684	20	10	0	4.3	80	0.3	NA	731b	461276	5.3	61
Mitsubishi Bank	9	58077	20	23	12	4.9	58	0.3	NA	999	403975	8.5	61
Dai-ichi Kangyo Bank	10	57375	18	16	5	4.2	87	0.3	NA	666b	464360	4.9	61
Sumitomo Bank	11	56387	18	1	-8	4.5	54	0.3	NA	1050b	462861	8.4	61
Sanwa Bank	12	49943	17	9	-1	3.9	61	0.4	NA	818b	442684	6.5	61
Mitsui Taiyo Kobe Bank	13	48692	15	-3	-12	4.4	53	0.4	NA	521	234019	8.3	61
Toyota Motor	16	44005	13	-13	-21	1.4	14	1.1	66553	3193	61037	10.4	42
Tokyo Electric Power	21	37528	28	-10	-18	3.7	88	1.3	31709b*	427b	77058	4.2*	12
Nomura Securities	23	30803	16	-5	-14	2.2	23	0.7	NA	1998	45023	9.6	62
Long-Term Credit Bank of Japan	27	29793	12	-8	-17	4.0	110	0.5	NA	270b	213089	3.6	61
Hitachi Ltd.	29	27729	8	-17	-25	1.4	17	0.9	56012b	1665b	61724b	8.2	34
Tokai Bank	34	26103	13	11	1	3.5	72	0.5	NA	362	281083	4.9	61
Matsushita Electric Industrial	37	25461	12	-15	-23	1.1	14	0.6	47781b	1875b	56838	8.0	41
Nippon Steel	41	23190	3	-18	-25	3.2	27	1.3	21523	847	30413	11.8	25
Kyowa Saitama Bank	44	21828	9	13	2	3.4	54	0.5	NA	226	112705	6.2	61
Kansai Electric Power	47	20623	21	-17	-25	2.8	51	1.7	16289b*	405b	40549*	5.6*	12
Bank of Tokyo	49	20461	10	7	-3	3.0	58	0.6	NA	355b	230862	5.3	61
Mitsubishi Trust & Banking	58	18477	14	0	-10	3.2	62	0.4	NA	298b	148954	5.1	62
Mitsubishi Heavy Industries	59	18210	5	-23	-30	2.9	26	1.1	18606b	702b	24882	11.3	38
Toshiba	60	18197	6	-21	-29	2.3	21	1.3	33990b	876b	37508	11.0	34
NEC	67	16705	11	-19	-27	2.7	42	0.6	26786b	394b	26671	6.3	34
Chubu Electric Power	72	15815	21	-12	-20	2.5	71	1.7	13248b*	224b	30877*	3.5	12
Sumitomo Trust & Banking	75	15572	13	-11	-20	2.7	47	0.5	NA	332b	137067	5.8	62
Sony	77	15443	46	-19	-27	1.4	18	0.8	26185b	847b	33316b	7.9	41
Tokio Marine & Fire	81	15098	10	-5	-14	4.1	56	0.6	7312b*	268b	30088	7.4*	63
Fujitsu	84	14824	8	-15	-23	1.9	25	0.8	21501b	599b	21509	7.6	33
Nintendo	86	14564	103	1	-9	10.6	29	0.3	3410b	499b	2480	36.3	46
All Nippon Airways	88	14414	10	-7	-15	10.5	131	0.4	5234	110	7837	8.0	56
Seven-Eleven Japan	90	14377	56	34	22	13.6	66	0.3	5647*	190	1638*	20.6	54
Mitsubishi Corp.	92	14259	9	-15	-23	2.9	30	0.6	142836b	473b	84544	9.7	59
Japan Air Lines	93	14228	8	-29	-35	4.7	111	0.4	9086	128	11992	4.3	56
Yasuda Trust & Banking	94	14133	13	1	-9	3.7	38	0.5	NA	365	104315	9.7	62
Daiwa Bank	96	13909	9	-2	-11	3.7	71	0.5	NA	239*	127670*	5.2	61
Nissan Motor	98	13600	5	-32	-38	1.1	38	1.9	43148b	355b	41591	2.8	42
Mitsui Trust & Banking	99	13531	11	4	-5	2.8	29	0.5	NA	469	111815	9.8	62
Nippon Credit Bank	100	13443	77	-30	-37	3.7	49	0.6	NA	275	131101	7.5	61
Daiwa Securities	102	13211	10	-12	-20	1.8	11	1.0	NA	1187	51386	16.0	62
Mitsubishi Estate	103	13204	10	-6	-14	4.4	40	0.5	2382	328	9754	10.9	64

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41	Ito-Yokado	105	12912	31	13	3	4.0	26	0.5	13248b	501b	6545	15.4	54
42	Tokyo Gas	106	12816	5	-15	-23	4.7	66	0.8	5408	194	8275	7.1	12
43	Sharp	110	12237	12	-4	-13	2.4	36	0.7	10859b	340b	14718	6.8	41
44	Mitsubishi Electric	115	11713	5	-16	-24	2.2	20	1.3	24006b	578b	22971	10.9	34
45	Asahi Glass	117	11652	10	-23	-30	3.1	34	0.7	8905	340	8880a	9.1	26
46	Fuji Photo Film	120	11466	25	-1	-10	1.7	18	0.4	7710	654	11072	9.9	46
47	Kirin Brewery	121	11440	11	-9	-18	3.2	37	0.5	10353	306	8630a	8.5	43
48	Nikka Securities	125	11146	8	-17	-24	1.7	12	1.3	NA	941	33939	14.7	62
49	Kobe Steel	129	11084	4	-7	-15	3.9	65	1.1	9600	169	15066	6.0	25
50	Seibu Railway	130	11042	25	-29	-36	26.4	268	0.1	3048	41	5249	9.8	57
51	Tokyu Corp.	131	10995	10	-22	-29	6.1	145	0.4	2700	76	7738	4.2	57
52	Kajima	134	10822	11	-14	-22	5.1	52	0.7	11467	207	16151	9.7	32
53	Sumitomo Metal Industries	135	10818	4	-13	-21	2.8	38	1.2	13067	282	16086	7.4	25
54	NKK	137	10739	3	-34	-40	3.0	38	1.2	10497	284	20264	7.9	25
55	Toyo Trust & Banking	138	10412	13	7	-3	3.2	33	0.5	NA	312	67560	9.7	62
56	Bank of Yokohama	140	10367	9	13	2	3.2	75	0.4	NA	148*	98147*	4.3	61
57	Kawasaki Steel	141	10358	3	-22	-30	2.5	26	1.4	8789	405	13632	9.6	25
58	Tohoku Electric Power	142	10303	21	-3	-12	2.9	51	1.7	7732*	196	16608	5.6*	12
59	Takeda Chemical Industries	143	10301	12	2	-7	3.0	39	0.7	5024	267	6899	7.7	45
60	Nippondenso	146	10263	12	-18	-26	2.1	22	0.8	10946	457	10111	9.2	37
61	Osaka Gas	162	9583	4	-19	-26	3.7	62	1.0	4329	153	6820	6.0	12
62	Honda Motor	163	9506	10	-17	-25	1.2	17	1.0	31130b	552b	19496	7.1	42
63	Kyushu Electric Power	164	9503	20	-3	-12	2.6	49	1.8	7717*	188	22001	5.4*	12
64	Fanuc	165	9481	40	-14	-22	3.6	38	0.3	1318	246	3146	9.3	35
65	Nippon Oil	166	9403	8	-7	-16	2.6	55	0.6	18207	169	15913	4.7	11
66	Kinki Nippon Railway	169	9378	6	-15	-23	6.5	76	0.6	5734	124	8210	8.6	57
67	Yamaichi Securities	175	9183	8	-20	-27	1.6	12	1.3	NA	789	33794	13.7	62
68	Mitsui & Co.	181	8925	6	-15	-23	2.0	30	0.9	150800b	297b	69616	6.7	59
69	Dai Nippon Printing	190	8730	12	-13	-21	2.1	29	0.8	7783	297	8079	7.2	52
70	Kyocera	191	8613	46	-11	-19	2.6	37	0.7	3337b	234b	4714	6.9	35
71	Sumitomo Corp.	199	8469	8	-9	-18	1.8	25	0.7	144921b	341b	40607	7.3	59
72	Mitsui Real Estate Development	202	8409	10	-21	-29	2.2	28	0.6	9122b	300b	21320	7.8	64
73	Sanyo Electric	204	8315	4	-35	-41	1.6	66	1.3	10657	127	14465	2.4	41
74	Shimizu	206	8268	10	-27	-33	4.2	41	0.6	11315	200	16180	10.1	32
75	Canon	208	8171	11	-5	-14	1.8	18	0.8	12510	445	13234	9.9	46
76	Shizuoka Bank	209	8133	10	20	9	3.8	68	0.4	NA	146*	56606	5.5*	61
77	Tonen	216	7910	12	12	2	2.8	55	1.5	5857	145	4942a	5.2	11
78	Asahi Chemical Industry	219	7785	6	-9	-17	2.8	25	1.1	9411b	309b	8685	11.2	22
79	Matsushita Electric Works	222	7745	12	-9	-17	3.0	32	0.7	7471	241	6219a	9.4	34
80	Kubota	224	7730	5	-25	-32	3.4	235	0.7	5944	55	7164	1.4	38
81	Sumitomo Electric Industries	229	7574	11	2	-8	3.4	33	0.6	8036b	229b	8149	10.2	37
82	Ajinomoto	238	7369	11	-18	-26	2.9	84	0.6	4300b	88b	5258	3.5	44
83	Taisei	241	7266	7	-24	-31	3.2	49	1.1	12090	149	16224	6.7	32
84	C. Itoh	243	7161	5	-20	-27	1.9	31	0.9	152016	228b	54803	6.1	59
85	Marubeni	246	7055	5	-15	-23	2.1	29	0.9	141606b	247b	62832	7.4	59
86	Hanwa	248	7012	19	-27	-34	2.7	42	0.5	5625	166	41533	6.4	54
87	Nippon Express	249	6968	6	-18	-26	5.9	53	0.7	11004b	131b	6764	11.0	57
88	Toppan Printing	250	6949	11	-11	-19	2.3	29	0.7	7066	240	6717	7.8	52
89	Ishikawajima-Harima Heavy Industries	251	6947	5	-32	-38	6.6	68	0.7	5835	102	8690	9.8	38
90	Chugoku Electric Power	253	6926	19	-9	-18	2.6	52	1.9	5871*	126	15507*	4.9	12
91	Sankyo	254	6909	17	13	2	5.4	73	0.4	3084	94	3054	7.4	45
92	Chiba Bank	255	6870	9	20	9	2.6	65	0.4	NA	121*	68103*	4.0	61
93	Daiwa House Industry	257	6816	14	-8	-17	3.3	29	1.0	4865	230	6967	11.4	32
94	Sekisui House	263	6683	11	-12	-20	2.0	21	1.2	7891b	319b	8024	9.3	32
95	Hokkaido Takushoku Bank	264	6671	7	-10	-18	2.6	46	0.7	NA	143	81858	5.7	61
96	Toray Industries	265	6648	5	-13	-22	2.3	24	1.1	6639b	272b	7652	9.7	22
97	Mitsubishi Kasei	266	6601	4	-11	-20	3.1	38	1.0	8354	173	10681	8.1	22
98	Komatsu	271	6419	6	-20	-27	1.8	28	0.9	6421	198	8909	6.4	38
99	Yamanouchi Pharmaceutical	272	6338	20	13	3	3.4	27	0.4	2223b	237b	4015	12.6	45
100	Sumitomo Chemical	283	6164	4	-19	-27	4.1	37	1.1	7746	166	7805a	10.9	22
101	Yasuda Fire & Marine	284	6163	7	-10	-18	4.1	53	0.7	5249b*	116b	22928	7.7*	63
102	Ohbayashi	287	6039	8	-29	-36	3.7	37	0.6	8391	162	11851	9.9	32
103	Joyo Bank	292	5987	8	-34	-40	3.0	50	0.5	NA	132*	62115*	6.0	61
104	Kawasaki Heavy Industries	294	5974	4	-32	-39	7.7	66	0.8	6660	90	7323	11.7	38
105	Hokuriku Bank	296	5957	9	4	-6	2.7	50	0.4	NA	119	63259	5.5	61
106	Bridgestone	299	5920	8	-27	-34	1.8	182	1.4	12886	33	11876a	1.0	37
107	Mitsubishi Materials	302	5833	5	-12	-20	3.2	34	0.8	5712	109	5999	9.6	24
108	KDD	303	5816	90	-19	-26	2.9	60	0.4	1745b*	98b	3545*	4.8	55
109	Marui	308	5735	16	-17	-25	2.4	23	1.0	4344b	249b	5068	10.3	54
110	Toyoda Automatic Loom Works	311	5708	20	1	-8	3.9	47	0.5	3562*	114	2482	8.2*	38
111	Nisshin Steel	320	5637	6	-14	-22	3.2	23	0.9	3323	243	6817	13.6	25
112	Nissan Fire & Marine	325	5617	28	-14	-22	19.3	206	0.2	1571*	27	5246	9.3*	63
113	Toyo Seikan Kaisha	336	5476	27	29	17	3.0	24	0.2	5104	224	4100	12.1	26
114	Shikoku Electric Power	338	5448	20	-5	-14	2.7	38	1.8	2881*	135	7802	7.1*	12
115	Ashikaga Bank	343	5339	9	10	0	3.0	51	0.5	NA	129*	49938*	6.0	61
116	Mitsui Marine	345	5303	7	1	-9	3.8	51	0.7	3526b*	104b	15608	7.5*	63
117	Daishowa Paper	346	5271	25	11	1	7.7	137	0.2	2889	38	5813	5.7	23
118	TDK	347	5265	41	-6	-14	2.1	26	0.8	3909b	206b	4434	8.3	35

Footnotes on page 57

Tables continued on page

How First Chicago stays steady when interest rates don't.

In theory, the banking business is pretty straightforward. Buy money at one price and sell it at another (hopefully higher) price. But in reality, buying and selling billions of dollars amidst interest rate gyrations can make it hard to stay on track.

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Mazda Miata It may have been thirty years ago, or just yesterday. A little two-seater caught your eye, and you've never been quite the same. Memories like this created the Mazda Miata. A product of both dreams and advanced technology, it's the perfect reason to pursue your love of the classic sports car.

Slip into the cockpit and you're greeted by snug, supportive seats and traditional round analog gauges. Twist the key and the 1.6-liter DOHC engine answers with a throaty growl—a note tuned to perfection by testing more than 100 exhaust pitches.

As you snap through the gears with the short-throw shifter, the front-engine/rear-drive layout and four-wheel double-wish-bone suspension combine to deliver razor-sharp handling. There's little doubt that the Miata is a purist's dream.

Yet this is one dream car that's also thoroughly down to earth. It may well be the most trouble-free sports car you'll ever own.

Even the most jaded critics have fallen head over heels. Every major automotive magazine judged Miata to be one of the best cars in the U.S. In fact, *Road & Track* named it "One of the Ten Best Cars In The World."* Kind of makes it hard to resist, doesn't it?

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To Panasonic, being an official sponsor of the 1992 Summer Olympic Games is both a commitment and a challenge. We've dedicated our vast resources to improving the Games, its athletes, as well as your ability to enjoy them.

TAKING ATHLETES FURTHER

At the U.S. Olympic Training Center an athlete's performance is measured in inches, in seconds

and in infinite detail on Panasonic video equipment. The Olympic Training Centers across America have been provided with video equipment that can help athletes visualize, analyze and scrutinize every motion and subtlety to edge a 9.9 performance up to a 10.

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While the 1992 Summer Games take place in Barcelona, Spain, people all over America will feel as if the events are being held in their hometown. One reason: A wide range of Panasonic digital video equipment will help cover the Games. Including the world's first 1/2" digital videotape recorders and cameras. Small and lightweight, this equipment allows more spontaneous coverage. It lets broadcasters record and edit events with almost no visual deterioration, and can record higher quality audio and video images than standard analog equipment.

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The spirit behind the Olympic Games, the relentless drive and striving to improve, is at the core of what we call Human Electronics. Every day we dedicate ourselves to creating and marketing products that make life richer, safer and more comfortable. This dedication results in a single-minded philosophy: Don't create technology for technology's sake, but for man's sake.

Panasonic
MATSUSHITA ELECTRIC



The odd couple of the late 20th century global economy are at it again. As happens almost every year, the bickering between Japan and the U.S. seems to start in the spring and get worse with the hot summer weather.

There Are Phony Issues . . .

This year the gulf war started things off early. The Japanese government first looked indecisive over its contribution, then came across as penny-pinching in making a \$9 billion second installment, after chipping in \$4 billion earlier.

Japan's U.S. critics, by contrast, appeared unfair, demanding that Japan violate the constitution the U.S. imposed after World War II — as well as silly, since Japanese components are now vital to U.S. military hardware.

. . . And Real Ones

Nevertheless, on more substantive matters, each has plenty to complain about. The Japanese construction market, to take one U.S. issue, is not only closed but also a cartel shielded by the government bureaucracy.

The U.S., to cite a recent Japanese complaint, has pushed Japan to make difficult structural changes without taking corresponding tough action on the budget deficit.

But The Winner Doesn't Always Take All

Ironically, Japan has actually come off better in this battle of words so far. While U.S. politicians have preferred criticizing Japan to making

Cooperation and Contribution



Matsushita staffers joined in the 30th anniversary parade for Peachtree City in Georgia.

hard choices at home, Japan has been forced to modernize its economy — to make itself more competitive in the long term by eliminating structural inefficiencies.

Meanwhile as Barry Bluestone and Bennett Harrison observed almost a decade ago in *The Deindustrialization of America*, the U.S. has seen the dismantling of much of its industrial structure.

Japan Tries To Make Its Contribution

One consequence of trade friction has been a conscious effort by Japanese business to improve its image in the U.S. through philanthropy.

Recognizing that public service is a norm in the U.S., many Japanese companies now encour-

age employees to take part in community affairs. NEC, for instance, sponsors the U.S. Davis Cup team.

Corporate philanthropy has also increased with about \$500 million, compared with \$30 million five years ago. Major companies such as Matsushita, Hitachi, NEC, and Toshiba have set up foundations.

The Trade Imbalance Has Improved . . .

U.S. pressure has compelled Japan to open its markets more fully. This helped reduce the bilateral trade imbalance last year to about \$40 billion, compared with some \$57 billion in 1987.

Even this surplus should decline further. Many of the market-opening measures announced

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in the 1980s are only now beginning to take effect. Quotas on beef have been removed. Despite high tariffs, U.S. and other foreign beef is competitively priced and should capture a large share of the \$1.5 billion Japanese beef market.

More and more U.S. companies are able to penetrate the Japanese market. Microsoft has reportedly increased sales threefold in the last three years. Companies as diverse as Levi Strauss, Amway and H.J. Heinz do well there. Japanese companies have also contributed to the improving trade balance both by

shifting substantial production overseas and by increasing imports. Notes Toshiba Senior Executive Vice-President Kinichi Kadono: "Most major Japanese companies try to increase their imports by 15% a year."

... Yet Basic Problems Remain

Even so, Hitachi Chairman Katsushige Mita believes it will take at least another five years to overcome the Japan-U.S. trade imbalance, and until that happens, progress on other issues will be difficult.

Fundamental issues persist. Some are highly emotional. "The rice issue is ridiculous," asserts Hotel Okura Managing Director Goro Yamazaki. "The Japanese consumer wants foreign rice."

Then there is the distribution system, which the Japanese government has begun to tackle by liberalizing regulations on large stores. "The multilayer distribution system," suggests Mitsubishi Kasei President Masahiko Furukawa, "is a job-creating device left over from the time of the Shoguns. It is no longer justified and is bound to disappear."

High-tech products, especially in electronics and semiconductors, probably pose the greatest long-term threat to Japan-U.S. trade relations.

NEC President Tadahiro Seki-



Hitachi's latest mag-lev prototype developed with the Railway Technical Research Institute.

moto questions the motives of Japan's critics, pointing out the vital contribution Japanese high-tech suppliers make to U.S. manufacturers.

Matsushita Electric Industries Board Member and Managing Director Koju Suzuki suggests that part of the problem may be the decline of the U.S. electronics industry. While there are many electronics companies in Japan,

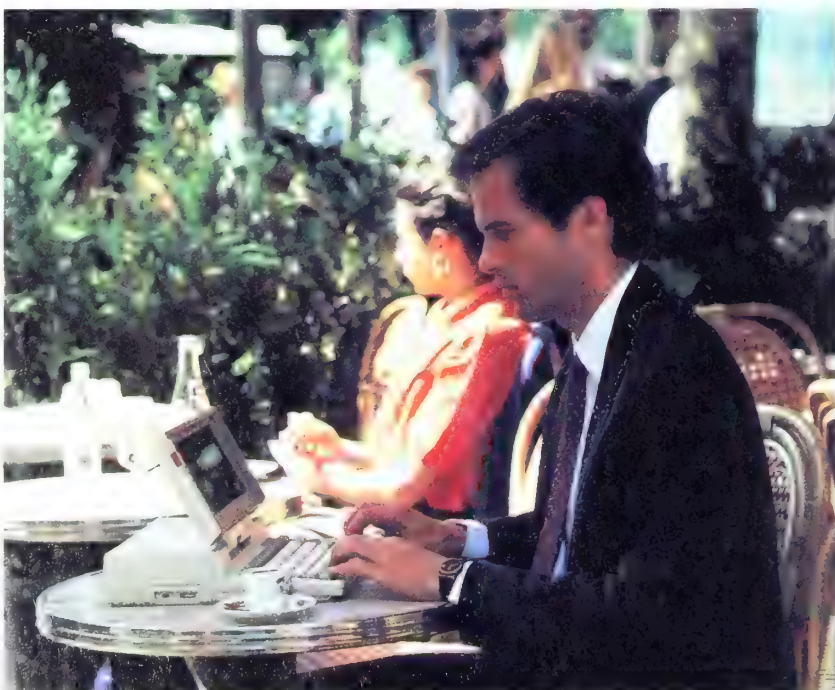
there are comparatively few in the U.S. "The solution seems to be to produce as many products in the U.S. as possible," he says.

"Trade friction will never go away entirely," warns Kikkoman Executive Managing Director Yuzaburo Mogi. "Japan has to continue to make an effort to open its market. We have to create an environment where even small U.S. companies can come and sell their products — the same kind of market the U.S. provided Japan in the 1950s and '60s. There should be no limit of trade competition."

Time To Grow Up?

While the U.S. needs to come to grips with the dismantling of much of its basic industry, Japan needs to take more responsibility for its own destiny. It should no longer rely on outside pressure to achieve the reforms domestic consensus cannot.

"Although Japan has become a global economic power," comments Komatsu President Tetsuya Katada, "it still has not yet established its political presence. This invites resentment. Japan must try to accommodate other governments. It must take the initiative." ■



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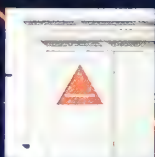
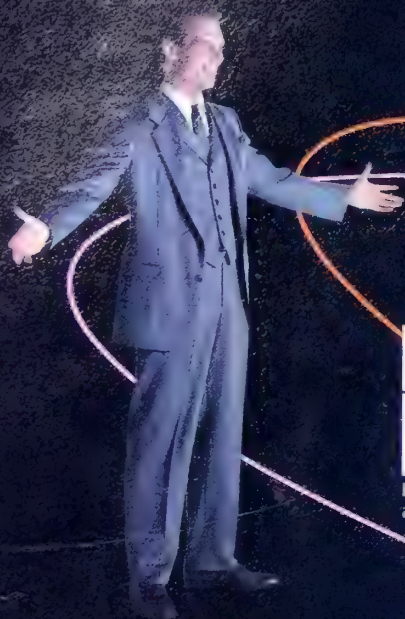


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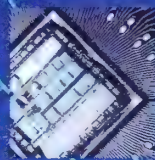
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Hitachi is a people company in other ways, too. Our recently established GREEN Center (Global Resources, Environment & Energy System Center) will soon join the battle to solve such problems as acid rain, the greenhouse effect and ozone depletion. Even more, we accept some 50 foreign researchers every year to work at our research laboratories. The international exchange of information that takes place leads to technological advances and stimulates further discussion among the academic community.

The breadth and scope of Hitachi is deep, indeed. Our products are found in offices, stores, factories, hospitals and homes around the world.

And with a people-oriented philosophy, Hitachi will continue to grow and secure a place as a citizen of the world. Creating products and technologies that make the lives of people everywhere better.

*US\$3,480 million, net R&D expenditures for the year ending March 31, 1991
US\$1 = ¥141



UNITED STATES & JAPAN

Like it or not, there is a global economy. Worldwide, businessmen are grappling with its implications.

As the struggle to remain competitive intensifies, national borders grow less important, and companies which think only in narrow nationalistic terms find they are losing out. Protectionist walls may postpone the reckoning, but not by much.

It is no longer enough simply to operate internationally; a company must be global in outlook. This is a lesson increasing numbers of Japanese companies are

learning. Japanese business began producing offshore both to ease worsening trade friction and to reduce rising production costs. But increasingly, Japanese companies find that it is not enough to plant factories around the world. In order to maximize the potential of this offshore investment, more coordination and sensitivity to the

CASE STUDY

NEC And "Mesh Globalization"

By Tadahiro Sekimoto, NEC President. "We had to develop our business outside Japan in order to grow."

Distinctive in its strength in computers, communications, and semiconductors, NEC put its first production facility abroad in 1958. Today, the company has 26 offshore manufacturing affiliates and

NEC has integrated its pro-

Beyond Internationalization:

Japanese Companies Aim to be Global in Outlook
As Well As Business



NEC's precise high-speed bonding technology is an important factor in semiconductor manufacturing.

duction on a global basis. Parts, sub-assemblies, and finished goods move from country to country for maximum production efficiency, in what Sekimoto calls "mesh globalization."

Supporting this integrative approach is a management philosophy that puts the emphasis not on instructions issued from Tokyo but on the interaction of the differ-

ent local parts of the company.

The company has delegated substantial authority to its offshore subsidiaries, which also have a better understanding of the local society and its needs.

What vitalizes this approach is a management style that seeks to integrate the individual and the company.

According to Sekimoto, NEC



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Only from a satellite's perspective can we hope to detect the Earth's many potential problems and prevent them from turning into uncontrollable disasters.

NEC's experience with satellites spans 30 years, and includes development of satellites for scientific, weather and Earth-monitoring purposes. In fact, NEC developed one of the first satellites to observe the Earth using visible light, infrared and microwave to make sure that even the most difficult to detect environmental problems won't go unnoticed.

Satellite observation has also come to play a vital role in such areas as agriculture, geology and marine sciences, just to name a few. But no field of study could have applications as important as monitoring global environmental conditions and keeping the most important patient's injuries to a minimum.



NEC Corporation is a leading global supplier of computers and communications systems and equipment. From marketing to research and development, while producing everything from satellites to semiconductors, our basis of operations is to promote a world of mutual understanding through the synergistic integration of "C&C" — computers and communications.





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wants to create a corporate culture that encourages voluntary action, innovation and awareness of the individual. Top management has worked with younger staff to streamline the corporate structure and internal communications to make this approach work.

CASE STUDY

Komatsu Prepares For An Industry Shift

When it comes to globalizing his company, Komatsu President Tet-suya Katada is impatient with his own headquarters. "I want to step up globalization in terms of the mentality of our staff," Katada says.

"It is actually lagging behind the rest of our operations," he adds. "Tokyo mainly uses only Japanese staff. That can limit the flexibility of people's thinking and their ability to do international business."

Katada puts a lot of emphasis on a global outlook because he believes the global construction industry is fundamentally unstable. A shakeout is overdue. It is essential to be ready for it.

Komatsu operates globally. It has production facilities in Southeast Asia as well as North and South America. Its aim internationally is to build a fully integrated vertical organization — from basic R&D and production to sales and marketing. Komatsu also pursues a strategy of horizontal alliances. It has linked up with Dresser Industries in the U.S. and Hanomag in Europe.

"We've established the minimum conditions needed to operate successfully in an unstable market," Katada says. "But in the long term, the company must be more aggressive in its approach to expansion and in establishing collaborative arrangements globally."

CASE STUDY

Nichimen

Founded in 1892 to meet the needs of Japan's emerging textile industry, Nichimen has grown to become a comprehensive trading

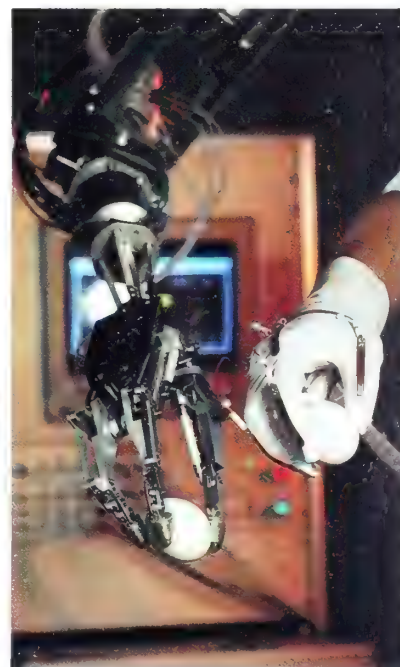
house, handling everything from textiles, lumber, chemicals, metals and fossil fuels to machinery, electronics and food products.

Compared with Japan's other *sogo shosha*, Nichimen focuses heavily on international trade. More than two-thirds of its sales involve overseas transactions. It is especially strong in third-country trade — which accounts for more than 40% of its turnover. Imports rank next at 17%, while exports total 11%.

The role of the Japanese trading company, however, is changing rapidly. Nichimen has moved beyond trade, building on its expertise to become a general trading company. It now offers clients support capability in marketing, finance, development capital, information services, technology and technology transfer, as well as mergers and acquisitions.

In Europe, through an affiliation with Britain's PA Consulting, it serves as an advisor in high-tech design and development. It has also established a Netherlands joint venture investment company, called Notis Europe, with British merchant bank Kleinwort Benson.

Nichimen supports its trading



Komatsu's Mighty Hand shown with a hand guide mechanism.



Nichimen America Inc. constructed the Pinnacle Peak Country Club.

activities and customer information service through its independent, high-speed, private communications network, Nichimex-90.

Where appropriate, the com-

pany takes a stake in strategic projects. Recently it founded a three-way joint venture investment company in Dalian, China. It has also formed an alliance with

Symbolics Corp. of the United States to found Japan Symbolics Corp., which sells artificial intelligence computers and software in Japan.

CASE STUDY

Matsushita Aims For True Globalization By The Mid-'90s

To meet the challenge of the global marketplace, Matsushita is reorganizing its 25 offshore subsidiaries and 20,000 employees into regional combines.

The company now divides the world into four regions: Japan, the rest of Asia, Europe and the Americas. Eventually, each will operate on a largely autonomous basis, with a regional holding company and supporting operating companies.

"The aim in each region is for Matsushita to be a local company from that region," explains Koju Suzuki, board member and managing director for corporate overseas regional coordination.



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Photograph by Pete Turner

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was ever achieved
without enthusiasm.”

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"We want the regional company to be an insider in its region," Suzuki explains. "Each will have its own production facilities, R&D, distribution, marketing and local management."

"Matsushita is willing to delegate local people to run these regional companies," Suzuki adds. The regional subsidiaries will submit business plans to Matsushita's

Osaka headquarters, which will monitor progress.

"The way to globalize is not to be Japan or Japan-employees oriented," Suzuki notes. Matsushita wants its subsidiaries run by local people who understand the company's corporate way of thinking.

CASE STUDY

Toshiba's Joint Venture Strategy

"In an era of globalization," remarks Toshiba Senior Executive Vice-

President Kinichi Kadono, "a company must view human resources on a global scale, and build a partnership with the communities we operate in."

Consequently, Toshiba puts increasing emphasis on having a management style that can match local needs. "In the '90s, the focus will be on society's needs as well as financial performance," Kadono adds.

To achieve this Toshiba is pursuing two strategic tracks. First, it is grouping its overseas operations in a tripolar structure based in North America, Europe and Asia.

This process is well advanced in North America. In the U.S., Toshiba has approximately 8,000 employees and \$3.4 billion in sales. Toshiba America, Inc., the holding company, coordinates the activities of 10 operating companies.

Toshiba's second globalization policy is to build complimentary links with other leading companies. "All companies need to maxi-

mize the use of their resources, and joint ventures offer benefits to all partners, in management, capital and technological collaboration," Kadono says.

Recent Toshiba joint ventures include a factory in France with GEC Ahlstrom to make and market vacuum bottles for vacuum circuit breakers, a semiconductor plant in Japan with Motorola and a marketing arrangement with General Electric to market appliances in Japan and explore optimized sourcing of consumer products throughout Asia.

CASE STUDY

Mazda Brings the *Kaizen* System to the U.S.

Mazda's *kaizen* system means continuous improvement. It involves an on-going team effort to upgrade productivity and quality. It is a concept that has been key to Mazda's success as an auto manufacturer both in Japan and in Flat Rock, Michigan.

Although productivity levels at the Flat Rock plant don't yet match those at the company's home plants, the quality levels match those in Japan.

Mazda has some 5,000 employees in the U.S. In addition, the plant has more than 110 suppliers. One of these is Ford, which has a long-standing relationship with Mazda and now makes the Mazda Navajo sport utility vehicle.

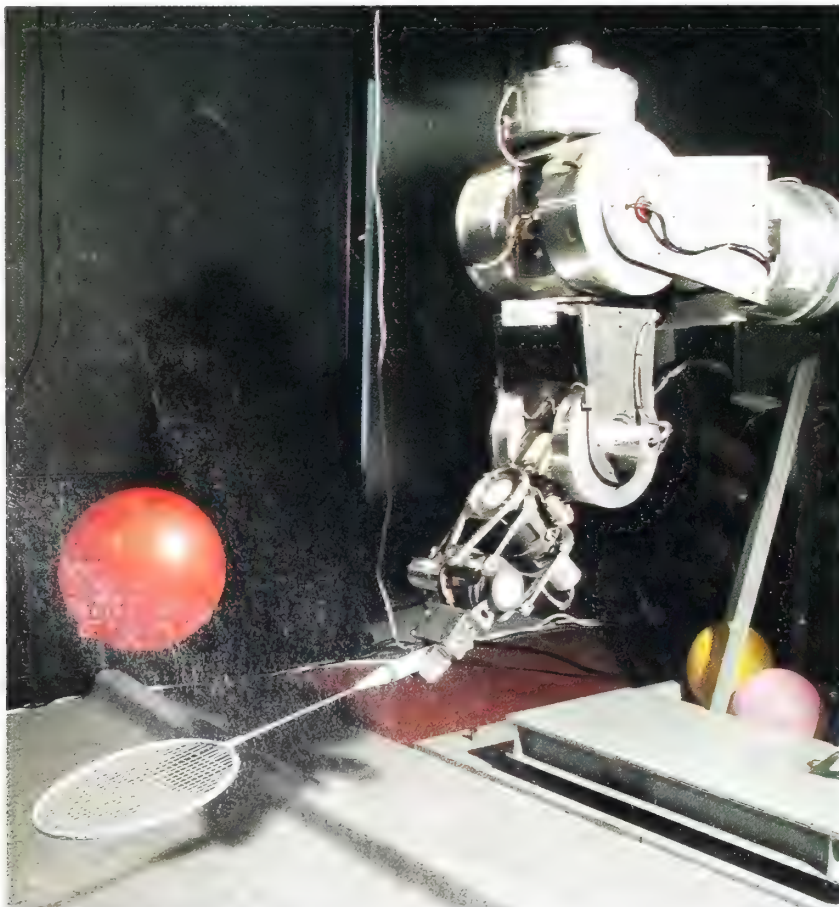
Overall, 65%-70% of the content of Mazda's U.S.-made vehicles is already domestic. The company's global objective is to increase the purchase of components from suppliers in countries where it has plants.

CASE STUDY

Hitachi Wants Independent Intelligence

According to Hitachi Chairman Katsushige Mita, 27% of the products Hitachi sells overseas are made there. By the mid-'90s, the company hopes to raise this ratio to 50%.

But with the growth of Hitachi's international operations has



Toshiba is developing multi-joint direct-drive robots with high-performance vision processors.



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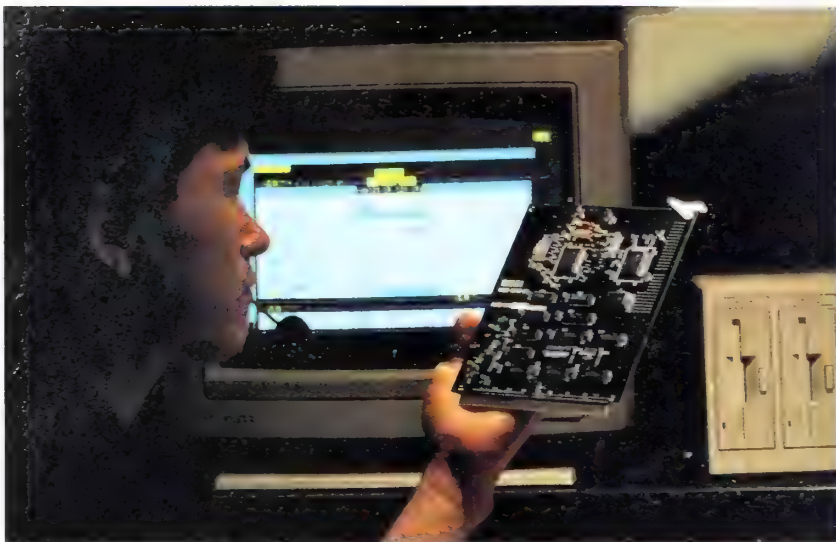
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come the need for what Mita calls independent intelligence. "Ten years ago, most of our divisions ran independently at home and abroad," Mita says. "Now, many more are active internationally, and there is need for more integration."

Hitachi has set up comprehensive overseas headquarters in Europe and the U.S. The aim is to attract top-quality managers abroad who can help Hitachi operate in a society different from Japan.

Hitachi also is encouraging its Japanese staff to learn more about other cultures. "I wish all of our employees working in Japan and the U.S. would deepen their understanding of the U.S.," Mita emphasizes.

"We want our overseas companies to be independent," Mita con-



Ricoh's voice recognition board for PCs uses fuzzy logic.

tinues. "We don't want them to have to rely on Tokyo.

"If these companies are nurtured," he adds, "we may well want to list their shares abroad." Hitachi would float some of the

shares, much as it is now doing on the Tokyo exchange with some of its Japanese subsidiaries.

CASE STUDY

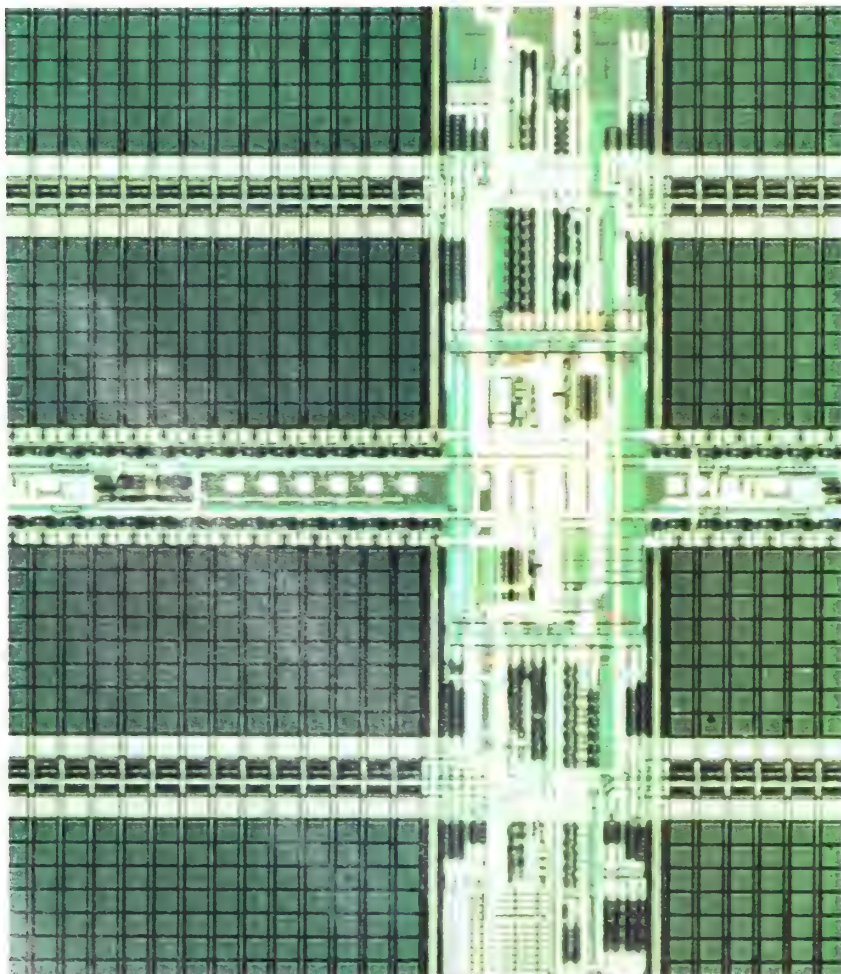
Ricoh Seeks Localization

Ricoh President Hiroshi Hamada is emphatic that true globalization is more than producing or shipping overseas to sell.

Ricoh has a long history of overseas production, first in Taiwan, later in the United States, then in Britain and France and soon in China's Shenzhen Special Economic Zone. Ricoh produces overseas both hardware and consumables, such as thermal paper and toners for its copiers. In fact, 90% of its consumable sales in the U.S. are supplied from local production.

But Hamada goes further. He sees the need to localize the product. "That means we have to have system-type R&D capability along with our overseas production," he says. "We also have to have good local managers."

Ricoh puts considerable emphasis on recruiting and training local managers. This effort has begun to pay off. At its three year-old French operation, more than half of the management staff are French. More than 80% of middle and upper management at Ricoh Electronics Inc. in California come from the local community. ■



Hitachi developed the world's first 64-megabit DRAM using 0.3-micrometer processing technology.



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All across Japan there are companies that are aggressively preparing themselves to be competitive in the 1990s and beyond. As the next century nears, they are all striving to ensure a prosperous future, as the following case studies will illustrate.

CASE STUDY

Komatsu Takes Down Its Bulldozer

For almost a quarter of a century, the symbol of Komatsu was a giant bulldozer atop its Tokyo corporate headquarters. Large enough to be a landmark, it signaled Komatsu's intention to be a major player in the construction equipment market.

Komatsu pulled the bulldozer down this year. In its place will be a high-tech news-and-information screen. The change symbolizes Komatsu's commitment to diversify.

During the 1980s Komatsu increased its nonconstruction equipment sales from almost nothing to 30% of its total. By the mid-'90s the company aims to have new business account for 50% of its total sales.

"Komatsu employees saw the bulldozer as a symbol," explains President Tetsuya Katada. "We want to put more emphasis on electronics, robotics and plastics."

Pushing to accelerate the pace of change, more resources are being committed to software, electronics, robotics, and plastics and to finding total engineering solutions. Katada expects that over the next three years sales will double, as Komatsu Electronic Metals expands into related devices.

In Search of the Corporate Fountain of Youth:

Japanese Companies Look to Diversification to Sustain Growth



Komatsu acquired part of the Husky Injection Molding Systems Ltd. of Canada.

Katada has also tackled Komatsu's corporate culture. "Staff transferred out of construction must no longer feel they are being demoted," he says. "We want them to see it as a promotion."

CASE STUDY

Kikkoman Opts For New Products

Kikkoman is an example of diversification through acquisition. The company is world-famous as a maker of premium soy sauce.

But the company also recognizes that the soy sauce market is

maturing. To counteract this, Kikkoman wants to expand its other processed food lines. It has acquired the Del Monte brand name in the Asia-Pacific region, excluding the Philippines, and will use it to develop new products for Japan and later the entire region.

CASE STUDY

Mitsubishi Kasei Has A New Name And New Products

In the 1970s, Mitsubishi Kasei — then called Mitsubishi Chemical — realized that fluctuating oil



Mitsubishi Kasei's newest drug Novastan®, an anti-thrombotic drug, is produced at the corporation's Kashima plant.

prices and unstable exchange rates put its highly cyclical traditional business lines at risk. The company realized it had to change.

It began to acquire basic R&D, especially in the life sciences. In 1980, the company laid down a ten-year diversification plan, calling for new products to generate 30% of sales by 1990.

By the end of financial year 1990-91 new products in biotechnology, pharmaceuticals, and information actually contributed 32% of total sales. Comments President Masahiko Furukawa. "By the mid-'90s we expect them to account for 40% of our sales and by the year 2000 50%."

The company has a number of new products coming on stream, including a plasminogen activator. "We will continue to invest in R&D," Furukawa emphasizes. "Every day we have to be innovative."

The company, however, has no intention of abandoning its traditional lines — which in good years yield an excellent return — and it continues to back research there as well.

Five years ago, Mitsubishi

Kasei adopted its new name, corporate identity and logo — partly to encourage the effort to make products that are more market-oriented.

More recently, it acquired Kodak's Verbatim disk business. Mitsubishi Kasei is now a world leader in floppy and hard disks. It also expects a big jump in optical disks. "We have invested heavily in this field," notes Furukawa, "and our production facilities are the world's largest."

CASE STUDY

Ricoh Responds To Changing Technology

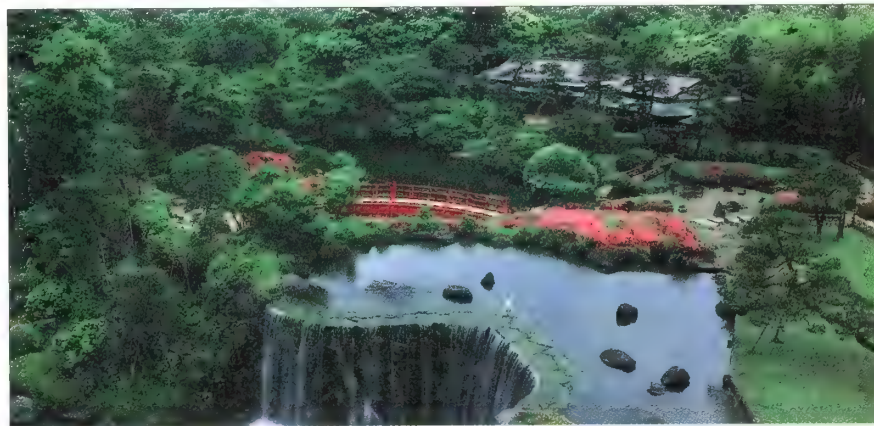
Looking ahead at the office of tomorrow, Ricoh President Hiroshi Hamada sees a world of paperless facsimiles, keyboardless computers and tightly integrated systems. "It will take time to get there," he says, "but as a company we must start setting up the preconditions necessary to be com-

petitive — in terms of R&D and product development."

The essential challenge, as Hamada sees it, is how best to help the customer handle information. This led Ricoh to the concept of Creative Office Architecture or COA — a play on OA, the Japanese code for office automation.

Key to Ricoh's approach is the belief that in tomorrow's office the corporate image processing system will be as vital as its data processing system is today. Digitalization will make this possible.

Part of Ricoh's strategy has been to link with other companies. Recently it teamed up with IBM Japan to develop connections between different equipment. But Hamada, for one, stresses that what works as a system in Japan may not work elsewhere. Systems even more than individual products must respond to local requirements. ■



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After all that has been written and said about the Japanese market in recent years, it is amazing how many foreign businessmen still arrive with misconceptions about the Japanese market.

They probably have learned a few lessons by rote. The Japanese appreciate quality, for example. And, they assume the Japanese market will be impressed by the quality of their products.

They cannot understand that in Japan there is not a different standard of quality, but a different definition and different price points. There are some products the Japanese esteem, which the rest of the world doesn't.

When failure inevitably comes, they are quick to blame it on the Japanese distribution system, on bias or on monopoly, not on their failure to do their homework first.

The Japanese market is difficult, but it can be mastered. "Marketing is the first step to doing business anywhere," says NEC President Tadahiro Sekimoto. "Two or three decades ago, Japanese companies learned market research from the U.S. and applied it."

Matsushita Electric Industrial Managing Director Koju Suzuki emphasizes, "For any foreign product to do well in Japan, it has to be modified to suit the Japanese market."

CASE STUDY

Hitachi Aims To Be More Market Oriented

The need to be aware of market trends is not restricted to foreign companies. Hitachi Chairman Kat-

Staying Ahead of the Market:

Mastering The Japanese Market the Japanese Way



Kikkoman's research is focused on biotechnology, enzymology and food science.

sushige Mita argues that for all his company's enormous success, it needs to be restructured to make it even more market-oriented. Now, the emphasis must be on products that are created in response to market demand — or even in anticipation of market demand.

"There will have to be a lot more emphasis on generating ideas," Mita says. That means that the engineering staff — traditionally one of Hitachi's great strengths — will have to become

more marketing-oriented. "The same people can do the job," Mita insists, "but they will have to shift their way of thinking."

CASE STUDY

Kikkoman Tracks Market Trends

Companies that want to be successful in the Japanese market must constantly track market trends and modify their products accordingly.

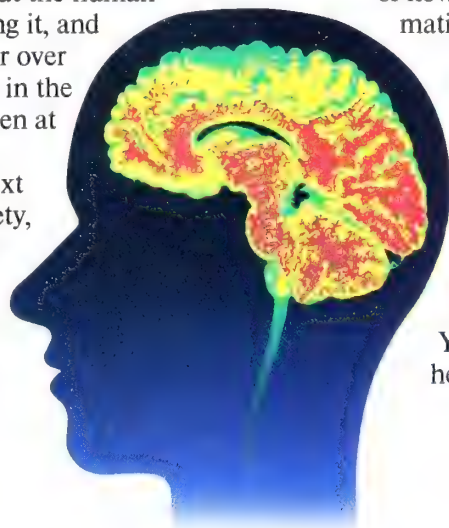
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Nikkei Business Publications is Japan's largest business magazine publisher.

different trends, comments Executive Managing Director Yuzaburo Mogi.

First, as the number of working women increases, there is a growing preference for convenience foods. Second, with rising affluence, gourmet cooking at home is gaining popularity.

Complicating these trends are shorter product life-spans and greater concern about packaging and the environment.

CASE STUDY

Hotel Okura Modernizes To Meet Changing Market Conditions

The Hotel Okura is well on the way to completing a total renovation of its facilities. To date, the program has cost more than \$50 million. Guest rooms, restaurants, and public areas have all been upgraded.

But the biggest changes are behind the scenes. With rising operating costs and a growing labor shortage, the challenge facing a hotel like the Okura, which prides itself on being one of the world's best, is how to offer its guests the service they want with fewer employees.

The Okura's solution is to make the maximum use of high technology. "We're spending money to install labor-saving equipment," says Managing Director Goro Yamazaki. "We know it will pay off."

CASE STUDY

Nikkei Business Publications Grows To Meet The Needs Of A Changing Economy

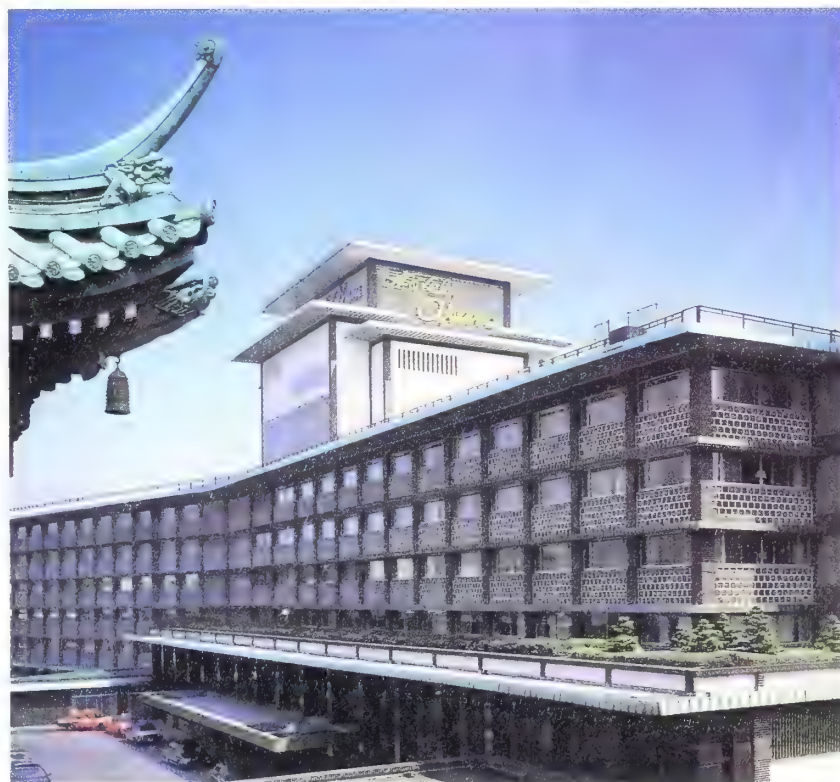
The growth of Nikkei Business Publications — Japan's largest business-magazine publisher and a leader in advertising revenues — mirrors that of the modern Japanese economy. *Nikkei Business*, its flagship publication, was founded just as the Japanese economy was taking off.

Today, the company publishes 26 magazines, which cover high-tech and service industries. In September it will launch the 27th, *Nikkei Executive Life*, reflecting the further maturing of the Japanese economy.

Nikkei Business remains Japan's most influential Japanese-language business magazine. Correctly using its superb penetration — like that of the newspapers published by the Nihon Keizai Shim-bun, Nikkei Business Publications' parent — is one of the keys to successful marketing in Japan.

Nikkei Business is now a weekly. "It was partly as response to the trend to a five-day work week," comments President Akira Nagata. "Our readers need to follow events closely and we can now help them get information in perspective on the weekend." ■

The text of this special advertising section was written by Christopher S. Gray, PhD. Gray is an expert on business in Asia and a frequent visitor to Japan.



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Toyo Sash	356	5174	24	-5	-14	3.0	29	0.2	2983	177	3817	10.4	21
Pioneer Electronic	357	5174	29	-27	-34	2.5	21	0.6	4344b	248b	3361	11.8	41
Kao	364	5071	9	-9	-17	2.7	35	0.6	4793b	145b	4147	7.7	44
Hitachi Zosen	365	5064	5	-14	-22	10.2	488	0.0	2490	10	3236	2.1	38
Hachijuni Bank	367	5039	9	11	1	3.5	55	0.4	NA	103*	41953*	6.3	61
Taisho Pharmaceutical	368	5038	16	7	-3	3.9	31	0.9	1252b*	161b	1915	12.3*	45
Odakyu Electric Railway	369	5037	8	-10	-19	5.5	114	0.5	2592	44	4740	4.8	57
Mitsubishi Motors	377	4908	6	-8	-16	2.0	32	0.8	17093	153	12821	6.3	42
Bank of Fukuoka	385	4839	8	6	-4	2.9	43	0.4	NA	127*	47057*	6.8	61
Fuji Electric	395	4730	7	-9	-17	4.4	29	0.9	6067b	161b	5645	14.9	34
Mitsui O. S. K. Lines	398	4709	4	-29	-35	4.6	47	0.6	3482	100	5947	9.8	58
Sumitomo Metal Mining	399	4708	9	-12	-20	3.9	34	0.5	4308	139	4156	11.6	24
Isetan	400	4683	21	-17	-25	4.7	77	0.3	3511	61	2795	6.1	54
Sumitomo Marine & Fire	402	4675	7	-3	-12	3.2	44	0.7	2773*	107	13922	7.3*	63
Mazda Motor	403	4672	4	-28	-35	1.6	24	1.3	19619b	193b	10011	6.8	42
Sekisui Chemical	404	4666	9	-15	-23	2.2	21	0.6	5147	219	6567	10.2	21
Matsushita Communication Industrial	408	4626	25	3	-7	3.7	56	0.3	2831	83	2099	6.7	34
Secom	411	4540	44	10	0	4.7	44	0.4	398c	34	2021	10.8	52
Mitsukoshi	422	4422	9	-27	-34	5.3	84	0.5	7225	52	2917	6.3	54
Toto	426	4398	13	-10	-19	3.3	34	0.6	2519	130	2543	9.7	21
Hokuriku Electric Power	442	4275	20	-8	-16	2.3	35	1.8	2671*	113	7586*	6.4	12
Shiseido	444	4260	14	-4	-13	2.3	37	0.6	3743b	115b	4250	6.1	45
Asahi Breweries	445	4260	10	-19	-26	2.2	190	0.4	6356	22	8522a	1.2	43
Gunma Bank	451	4229	8	7	-3	3.1	67	0.4	NA	92*	35930*	4.6	61
Fujisawa Pharmaceutical	452	4217	13	-4	-13	2.7	94	0.4	1665	44	3762	2.9	45
Nagoya Railroad	453	4207	6	-20	-28	4.2	68	0.6	2432	62	7888	6.2	57
Keio Teito Electric Rail	455	4178	7	-5	-13	5.5	86	0.5	2932	49	4102	6.5	57
Fujita Corp.	457	4148	8	-15	-23	3.5	47	0.8	4995	89	8782	7.4	32
Hankyu Corp.	458	4142	5	-26	-33	3.7	61	0.7	2259	68	5464	6.0	57
Daichi Pharmaceutical	460	4134	15	-4	-13	3.6	26	0.5	1484	158	2422	13.9	45
Teijin	462	4117	4	-17	-25	2.0	22	1.2	4438b	190b	6503	9.4	22
Bank of Hiroshima	463	4115	7	-17	-25	3.0	50	0.5	NA	89*	45204*	5.9	61
Hokkaido Electric Power	468	4076	19	-12	-20	2.5	44	1.9	3258*	88	9752*	5.8	12
Nippon Mining	469	4067	5	-35	-41	3.6	215	0.8	7355	19	7345	1.7	11
Kumagai Gumi	472	4062	6	-26	-33	1.6	36	1.1	8593	112	15196	4.5	32
Kyowa Hakko	474	4039	9	1	-9	4.0	59	0.5	2295	68	2955	6.7	45
Tokyo Steel Mfg.	477	4027	27	3	-6	4.5	16	0.5	1687b*	256b	1778	28.7*	25
Tokyo Electron	479	4008	27	7	-3	4.3	49	0.3	1376	80	1542	8.8	35
Kyushu Matsushita Electric	488	3951	23	9	-1	6.0	54	0.3	1759*	66	1446	11.0*	41
Matsuzakaya	491	3913	25	-49	-54	8.1	57	0.2	3866	68	1707	14.1	54
Murata Mfg.	492	3902	19	12	1	1.8	21	0.6	2005b	182b	2995	8.6	35
Showa Denko	493	3900	4	-29	-36	4.1	63	1.2	4561	62	4628a	6.5	22
Furukawa Electric	500	3859	6	-8	-17	2.9	71	0.7	5546	54	5228	4.2	37
Oji Paper	502	3853	6	-19	-26	2.2	31	1.0	4851b	125b	5402	7.1	23
Isuzu Motors	503	3843	4	-45	-50	3.4	LOSS	1.0	11004	-56	7475a	NEG	38
Shin-Etsu Chemical	505	3838	12	7	-3	2.6	19	0.5	3077	201	3953	13.8	22
Daiei	506	3833	10	-32	-39	4.0	55	1.2	16506b	69b	8040	7.3	54
Chiyoda Corp.	517	3759	19	9	-1	5.9	116	0.2	1745	33	2408	5.1	38
Mitsui Engineering & Shipbuilding	522	3723	5	-29	-35	5.6	143	0.6	1672	26	3700	3.9	38
Nippon Light Metal	538	3644	7	21	10	7.6	38	0.5	4170	88	3988	19.8	24
Omron	539	3644	16	-8	-17	2.3	24	0.6	3012	151	3337	9.7	34
Jusco	540	3636	12	-21	-29	2.5	33	1.2	9781	111	5981	7.8	54
Nippon Fire & Marine	542	3614	6	-22	-29	2.8	45	0.8	2367*	80	11605	6.1*	63
Ono Pharmaceutical	543	3613	29	-19	-27	5.9	74	0.3	167c*	32	1267	7.9*	45
Ricoh	545	3608	6	-25	-32	1.4	37	1.3	7240b	98b	6020	3.9	33
Ube Industries	552	3526	4	-12	-20	5.9	23	0.9	4525	153	6106	25.4	26
Keihin Electric Express Railway	558	3486	7	-11	-19	5.3	90	0.5	1585	39	3804	5.9	57
Nikon	560	3479	9	-11	-19	3.5	25	0.7	2056	136	2465	13.6	46
Nissho Iwai	561	3462	4	-28	-35	2.2	41	0.8	111793	133	36900	5.3	59
Tokyo Dome	562	3456	24	-3	-12	6.0	100	0.4	642	34	3202	6.0	53
Takashimaya	563	3438	16	-21	-29	5.5	29	0.5	7486	119	4202	19.3	54
Cosmo Oil	565	3413	6	-11	-19	5.3	49	0.6	11069	69	8779	10.9	11
Hyogo Bank	568	3386	10	-17	-25	3.1	89	0.4	NA	57*	29443*	3.4	61
Ebara	572	3360	12	-19	-27	4.4	170	0.5	1991	20	2450	2.6	38
Mitsubishi Petrochemical	578	3348	7	-15	-23	2.6	14	0.9	3251	236	4738	18.1	22
Sumitomo Realty & Development	583	3295	8	-20	-27	2.0	26	0.8	1817	125	10274	7.5	64
Daikin Industries	584	3291	13	-2	-11	4.2	28	0.7	3041b	119b	2343	15.3	38
Kinden	586	3285	20	9	-2	2.9	37	0.3	2794*	85	2894*	7.8	32
Kokuyo	590	3272	25	-7	-16	4.0	32	0.4	1122c	51	1854	12.7	52
Hitachi Metals	591	3271	9	-7	-16	2.9	43	0.8	3041	75	3296	6.7	25
Sumitomo Heavy Industries	596	3239	6	-16	-24	6.2	82	0.5	3171	40	3917	7.6	38
Hitachi Cable	600	3213	9	12	2	3.0	32	0.8	2823b	99b	2232	9.3	37
Nichii	602	3198	12	-25	-32	2.3	31	1.2	8021	103	6121	7.4	54
Nippon Seiko	606	3169	6	-23	-30	1.9	29	1.0	2773	111	4296	6.7	37
Bank of Kyoto	608	3162	13	-16	-24	4.9	60	0.3	NA	61*	24578*	8.1	61
Oki Electric Industry	609	3160	5	-25	-32	2.4	44	1.0	4785b	72b	5105	5.4	34

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COUNTRY RANK		GLOBAL 1000 RANK	MARKET VALUE U.S. \$ MIL.	PRICE PER SHARE U.S. \$	% CHANGE FROM 1990 (U.S. \$) (LOCAL)		PRICE-BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL.	PROFITS U.S. \$ MIL.	ASSETS U.S. \$ MIL.	RETURN ON EQUITY %	INDUSTRY CODE
197	Dainippon Ink & Chemicals	615	3141	4	-17	-25	2.3	53	1.1	5813	59	6285	4.3	22
198	Keisei Electric Railway	620	3107	11	-7	-16	89.6	38	0.3	1318	81	2223	234.4	57
199	Koito Mfg.	622	3100	19	-6	-15	7.0	92	0.3	1296	34	1001	7.6	37
200	Eisai	623	3098	13	9	-2	3.0	30	0.5	1484b*	104b	2036	10.1*	45
201	Sapporo Breweries	625	3094	9	-11	-19	3.4	121	0.4	3714	26	4370a	2.8	43
202	Showa Shell Sekiyu	634	3064	11	29	17	6.5	42	0.4	12162	74	5376a*	15.6	11
203	Dai-Tokyo Fire & Marine	636	3063	8	-7	-15	2.6	47	0.7	2382*	66	9136*	5.6	63
204	NGK Insulators	644	2994	8	-20	-28	2.9	45	0.7	1578	66	1968	6.3	37
205	Mitsui Toatsu Chemicals	645	2987	4	-21	-28	2.8	26	1.1	3620	117	5212	10.8	22
206	Hasegawa Komuten	663	2907	7	-22	-30	1.4	31	1.1	3837	95	8384	4.6	32
207	Kuraray	665	2899	11	6	-4	4.1	44	0.5	2237	65	2636	9.4	22
208	Mitsubishi Oil	672	2875	8	-1	-10	4.9	80	0.5	5712	36	5270	6.2	11
209	Shionogi	673	2873	8	-23	-30	2.3	32	0.7	2165	89	2476	7.2	45
210	Nichido Fire & Marine	674	2870	7	-8	-16	2.8	43	0.8	2237*	66	11279	6.5*	63
211	Nishi-Nippon Bank	675	2870	7	-1	-11	2.7	64	0.5	NA	58*	27300	4.2*	61
212	Orient	681	2853	8	-7	-15	1.6	28	1.0	NA	117*	41874	5.7*	62
213	Toyobo	682	2841	4	-25	-32	3.9	49	0.9	3779	58	4066	8.0	47
214	Yamazaki Baking	686	2823	13	7	-3	2.8	38	0.6	3345	75	1935a	7.5	44
215	Victor Co. of Japan	688	2814	11	-34	-40	1.4	24	0.8	6704b	116b	4603	5.6	41
216	Seiyu	689	2813	14	2	-7	4.1	35	0.8	9267b	80b	9537	11.6	54
217	Honshu Paper	690	2802	8	-51	-56	4.6	73	0.5	3243	38	4105	6.3	23
218	Kankaku Securities	696	2775	7	-32	-38	1.4	16	1.0	NA	163	8050	8.8	62
219	Tokyo Broadcasting System	697	2771	16	-18	-26	2.5	27	0.5	1571b*	102b	1700	9.1*	51
220	Konica	698	2767	8	-24	-31	2.3	398	0.9	3685	7	3980	0.6	46
221	Fukuyama Transporting	717	2671	10	7	-3	3.5	55	0.7	1376*	62	1638*	6.3	57
222	Yakult Honsha	719	2665	15	-7	-16	2.5	27	0.7	1122	96	1605	9.2	44
223	Sankyo Aluminium	725	2656	11	-1	-10	5.7	49	0.4	1745	53	1646a	11.6	21
224	Casio Computer	726	2653	10	-7	-15	2.6	40	0.9	2425b	66b	2605	6.6	46
225	Nissin Food Products	727	2651	20	-6	-15	2.2	36	0.9	1397b	72b	1918	6.1	44
226	Sato Kogyo	728	2650	10	-19	-26	6.9	84	0.4	1672c	16	4197	8.2	32
227	Yamato Transport	732	2642	10	9	-1	2.9	86	0.7	2896	29	1821	3.4	57
228	Tomen	733	2641	4	-28	-35	3.1	43	1.0	51271	61	15608	7.2	59
229	Chugoku Bank	735	2638	13	-9	-18	2.0	46	0.3	NA	88*	29936*	4.3	61
230	Fujikura	737	2634	8	14	4	3.5	56	0.6	2013	47	2409	6.3	37
231	Seventy-Seven Bank	738	2632	7	-4	-13	2.8	50	0.5	NA	71*	27872	5.6*	61
232	Arabian Oil	743	2617	50	-20	-27	7.1	LOSS	0.6	1528a	-11a	1174a	NEG	11
233	Tokyu Department Stores	745	2606	9	-21	-28	3.1	60	0.6	3243	42	2734	5.1	54
234	Advantest	746	2602	35	7	-3	3.8	66	0.3	559	38	1115	5.7	35
235	Kandenko	749	2594	22	-2	-11	3.7	35	0.2	3156*	69	2265*	10.6	32
236	Tosoh Corp.	753	2585	5	-9	-17	3.6	461	0.8	2027	5	3767	0.8	22
237	Seino Transportation	754	2583	17	26	15	2.2	33	0.6	1926	77	2050	6.6	57
238	Daikyo Kanko	755	2576	14	-36	-42	1.8	20	1.6	5111b*	126b	10483*	8.6	64
239	Hino Motors	757	2554	7	-3	-12	3.4	28	0.8	4756b*	90b	2540*	12.1	38
240	Okumura	759	2548	10	-18	-26	3.3	43	0.7	2273*	55	3142*	7.8	32
241	Nippon Shinpan	762	2541	8	6	-4	1.8	28	0.9	NA	91	41389	6.3	62
242	New Japan Securities	766	2535	6	-33	-39	1.4	12	1.2	NA	213	11648	12.0	62
243	Minebea	769	2521	7	-8	-17	1.9	237	1.3	1904	11	5973	0.8	37
244	NTN Toyo Bearing	774	2508	5	-13	-21	2.2	30	1.2	2317	82	3203	7.2	37
245	Yokogawa Electric	777	2496	10	-12	-20	2.1	33	0.6	1745	77	2301	6.3	35
246	Nippon Meat Packers	780	2478	12	-1	-10	2.3	39	0.7	4836	64	3100	5.8	44
247	Jujo Paper	782	2468	5	-12	-20	2.3	22	1.0	3989	111	4732	10.5	23
248	Yamaha	783	2467	13	0	-10	2.2	45	0.6	3685b	55b	3424	4.9	46
249	Nagasakiya	784	2467	17	-41	-47	5.5	74	0.5	3316	33	2941	7.4	54
250	Japan Radio	785	2466	20	5	-5	5.2	57	0.3	1390	43	1459	9.2	34
251	Banyu Pharmaceutical	786	2465	9	7	-3	2.3	46	0.6	688*	58	1406*	5.0	45
252	Kawasaki Kisen	792	2437	4	-34	-40	6.1	125	0.0	3294	19	3337	4.9	58
253	Makita	795	2430	15	-11	-20	2.1	36	0.9	608c	33	1620	5.7	34
254	Aoki	796	2429	6	-30	-36	1.6	38	1.0	2925	61	4887	4.3	32
255	CSK	799	2414	38	8	-2	2.6	60	0.2	679	40	1284	4.4	52
256	Mitsubishi Rayon	802	2412	4	-22	-29	2.7	51	0.9	2367	47	3383	5.2	22
257	Nippon Hodo	809	2387	20	5	-4	3.1	51	0.4	1846*	45	1661	6.0*	32
258	Toho Co.	816	2365	167	-29	-36	4.8	45	0.4	1057	52	1401	10.7	53
259	Dainippon Pharmaceutical	819	2363	15	-14	-22	5.4	67	0.4	760	35	1027	8.1	45
260	Nihon Unisys	823	2342	21	36	23	5.0	66	0.3	2179	36	2056	7.7	33
261	Japan Steel Works	825	2332	6	2	-8	6.6	20	0.5	934	117	1305	33.2	38
262	Amada	826	2329	8	-31	-37	1.5	18	1.8	1368	125	2726	8.0	38
263	Nihon Cement	827	2329	7	1	-9	2.4	29	0.7	2128	81	3356	8.2	21
264	Nippon Television Network	832	2306	183	-15	-23	3.2	32	0.4	1462	71	1303	9.9	51
265	Citizen Watch	833	2306	7	6	-4	2.4	33	0.8	2418	70	2398	7.4	46
266	Asin Seiki	834	2305	8	-21	-28	1.6	22	0.9	4966	102	3238	7.3	37
267	Nisshin Flour Milling	836	2302	11	6	-3	2.8	24	0.4	2563	89	1635	11.6	44
268	Canon Sales	839	2294	28	9	-1	2.4	37	0.3	2787a	61a	1853a	6.5	52
269	Fukuoka City Bank	840	2294	11	-15	-23	3.0	59	0.3	NA	51*	18468*	5.1	61
270	Seiko	841	2293	22	-34	-41	10.3	457	0.3	3099b	5b	2692	2.3	46
271	Hazama	844	2290	7	-29	-36	3.5	30	0.8	4974b*	77b	4623*	11.8	32
272	NCR Japan	848	2278	10	-16	-24	3.3	32	0.9	862*	72	929*	10.4	33
273	Toho Gas	849	2269	4	-15	-23	3.4	62	1.0	1455	37	2018	5.6	12
274	Matsushita-Kotobuki Electric	851	2255	14	-10	-19	2.1	31	0.6	1984b*	74b	1498	7.0*	41
275	Mitsubishi Gas Chemical	852	2254	5	-18	-26	2.2	36	0.8	2071	62	2992	6.0	22

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Onoda Cement	860	2247	5	-18	-26	3.2	39	0.7	3048	57	4084	8.1	21
Tokyo Land	862	2232	5	-36	-42	2.8	75	0.7	1209c	15	5640	3.8	64
Daido Steel	868	2206	5	-19	-27	2.6	26	0.8	3171	84	3482	9.8	25
Nippon Sheet Glass	873	2194	5	-22	-29	2.5	28	0.9	1882	79	2870	8.9	26
Chiyoda Fire & Marine	874	2194	6	-16	-24	2.6	38	0.8	2143*	57	7474*	6.8	63
Fuji Heavy Industries	880	2182	4	-16	-24	1.1	LOSS	0.4	4785	-43	5989	NEG	42
Daifuku	889	2156	20	35	23	7.2	72	0.3	847	30	623	10.0	38
Kanebo	899	2139	4	-14	-22	12.7	241	0.8	4749	9	4690	5.3	47
Nippon Shokubai Kagaku Kogyo	900	2138	11	-13	-21	3.8	28	0.5	1137	76	1230a	13.6	22
Suzuki Motor	901	2135	5	-13	-21	1.5	52	1.1	7116	41	5110	3.0	42
Nippon Electric Glass	902	2135	15	-14	-22	3.1	46	0.5	1470*	73	2100	6.9*	37
Chugai Pharmaceutical	912	2120	9	-36	-42	2.8	232	0.6	941	4	1442a	1.2	45
Fujita Tourist Enterprises	915	2112	17	-36	-42	8.9	87	0.3	638	24	1002a	10.2	53
Sanyo-Kokusaku Pulp	916	2111	5	-9	-18	2.1	26	1.2	3424	80	3658	7.8	23
Penta-Ocean Construction	923	2101	7	-16	-24	7.1	72	0.7	2693*	25	2736	9.8*	32
Sagami Railway	939	2063	5	-32	-38	4.7	100	0.7	1231	21	2946	4.7	57
Alps Electric	941	2062	12	-21	-28	2.2	397	0.9	2918	5	3080	0.5	35
Inax	948	2050	9	-27	-34	1.8	31	0.7	1781*	66	1893*	5.8	21
Sanrio	949	2047	26	-38	-44	2.8	69	0.7	539c	19	2674	4.0	54
Nisshinbo Industries	954	2029	9	-4	-13	1.7	34	0.6	1795	59	2658	5.0	47
Uny	956	2027	11	-21	-28	1.7	28	1.2	4916	72	3172	6.1	54
Kakusai Electric	961	2018	28	-14	-22	6.2	45	0.4	825	44	639	13.6	34
Kurabo industries	964	2013	7	14	3	3.6	128	0.6	1086	16	1093	2.8	47
Maeda Corp.	969	1989	11	-16	-23	2.0	42	0.6	3062*	49	3520	4.8*	32
Meiji Seika	970	1988	5	-18	-25	2.6	39	0.9	2244	51	1589	6.7	44
Nichirei	972	1986	6	-16	-24	3.4	66	0.7	3366	30	2040	5.1	44
Olympus Optical	973	1983	9	-13	-21	2.0	33	1.1	1585	61	2318	6.0	46
Tanabe Seiyaku	978	1972	8	-9	-18	2.4	49	0.7	1737b	40b	1791	4.8	45
Niigata Engineering	982	1968	6	-6	-15	6.2	129	0.5	1549	15	1821	4.8	38
Maeda Road Construction	994	1944	20	3	-7	4.3	42	0.6	311c*	14	752	10.2*	32
Mitsui Petrochemical Industries	996	1940	6	-22	-29	2.0	14	0.9	2382	139	3290	14.5	22
Hokkaido Bank	998	1937	5	-19	-26	1.8	44	0.7	NA	52*	25223*	4.2	61
Daicel Chemical Industries	999	1933	5	-21	-29	2.1	27	0.8	1730b	71b	2813	7.7	22
Mori Seiki	1000	1930	20	-20	-27	2.3	21	0.8	683	90	1396	10.7	38

LAOSIA

ENTRY COMPOSITE		4211	2	-11	-15	2.9	27	1.6	1804	165	13189	10.9	
Sime Darby	857	2250	1	-6	-10	2.6	22	2.2	1804	103	1955	11.5	71
Malayan Banking	985	1961	3	-16	-20	3.2	31	1.0	NA	62	11234	10.3	61

THE NETHERLANDS

ENTRY COMPOSITE		94069	52	1	3	5.8	12	4.1	208916	9754	535343	38.9	
Royal Dutch Petroleum (1)	NR	43987	82	7	9	1.6	11	4.9	106479	6533	106431	14.0	11
Unilever NV (2)	NR	13518	84	4	7	4.9	15	3.2	39620	1980	14139	32.0	44
Internationale Nederlanden Group	282	6182	27	-18	-16	0.9	8	5.9	NA	809a	133915a	11.1	63
ABN AMRO Holding	366	5056	20	7	9	0.7	8	7.5	NA	661	201951	8.9	61
Philips Electronics	387	4822	16	-10	-8	0.8	LOSS	0.0	28652	-2177	26496	NEG	41
Polygram	611	3151	19	0	3	8.7	17	1.4	2697	183	2218	50.6	46
Elsevier	671	2875	45	-3	-1	10.8	16	2.4	1053	176	846a	66.0	51
Heineken	724	2660	83	23	26	1.6	14	2.2	3642	188	3843	11.6	43
Aegon	741	2624	62	-6	-4	1.1	7	5.9	3693	385	31045	17.1	63
Akzo	748	2598	58	-6	-4	1.1	8	5.7	8855	340	7025	14.1	22
Dordtsche Petroleum	763	2538	76	10	13	39.6	19	5.2	NA	133	64	207.9	11
DSM	953	2030	58	-6	-4	0.9	5	7.1	5219	417	5175	17.5	22
Ahold	955	2027	42	13	15	2.7	16	2.0	9006	125	2195	16.5	54

NEW ZEALAND

ENTRY COMPOSITE		2964	2	-11	-11	0.9	7	7.0	7760	425	10260	14.2	
Fletcher Challenge	652	2964	2	-11	-11	0.9	7	7.0	7760	425	10260	14.2	23

NORWAY

ENTRY COMPOSITE		6263	30	-4	0	2.7	13	2.1	9070	494	10472	21.2	
Norsk Hydro	276	6263	30	-4	0	2.7	13	2.1	9070	494	10472	21.2	11

SINGAPORE

ENTRY COMPOSITE		13585	6	10	5	1.9	17	1.5	2804	935	61857	11.9	
Singapore Airlines	381	4876	8	6	1	1.6	9	2.1	2804b	517b	4668	16.6	56
Development Bank of Singapore	547	3553	7	-4	-9	2.0	20	0.9	NA	162	29119	10.3	61
OCBC Overseas Chinese Bank	642	3002	5	9	4	2.2	24	1.2	NA	128	17812	9.2	61
United Overseas Bank	891	2155	4	29	23	1.9	17	1.8	NA	128	10258a	11.5	61

SOUTH AFRICA

ENTRY COMPOSITE	27182	18	7	5	2.4	13	3.8	2095	2696	12628	15.1		
De Beers Centenary	182	8921	23	-10	-11	NA	7	4.3	1494a	1195	NA	NA	26
Anglo American	228	7586	33	-1	-3	1.6	15	3.5	NA	534	6324	10.9	81
Gencor	467	4085	3	24	22	1.6	8	4.2	NA	513	2926	20.3	81

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THE GLOBAL 1000

COUNTRY RANK		GLOBAL 1000 RANK	MARKET VALUE U.S. \$ MIL.	PRICE PER SHARE U.S. \$	% CHANGE FROM 1990 (U.S. \$) (LOCAL)		PRICE/BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL.	PROFITS U.S. \$ MIL.	ASSETS U.S. \$ MIL.	RETURN ON EQUITY %	INDUS. CODE
4	Driefontein Consolidated	813	2374	12	6	4	3.3	13	4.3	601	174	884	24.8	8
5	Gold Fields of South Africa	903	2134	22	6	4	2.2	20	3.2	NA	128	1040	11.4	8
6	Johannesburg Consolidated	927	2082	14	16	14	3.1	13	3.3	NA	152	1454	22.9	8

SPAIN

COUNTRY COMPOSITE		58948	33	11	13	1.5	11	5.0	32348	5599	377571	14.4		
1	Telefónica Nacional de España	186	8801	9	21	24	0.8	13	5.4	7783	708	25510a	5.8	5
2	Banco Bilbao Vizcaya	234	7433	32	6	8	1.6	8	4.6	NA	945	78887	19.3	6
3	Repsol	237	7409	25	3	5	2.1	12	3.6	9542a	633	9152a	18.3	1
4	Banco de Santander	301	5836	53	17	19	2.1	10	3.8	NA	526	50009	19.9	6
5	Endesa	324	5618	22	-4	-3	1.3	8	4.7	5136a	745	12788a	17.7	12
6	Banco Central	416	4479	42	-11	-10	2.0	11	4.5	NA	376a	41581a	18.2	6
7	Banco Español de Crédito	513	3787	38	3	5	1.6	11	4.9	NA	355	47428	13.6	6
8	Iberduero	592	3261	7	8	10	0.6	11	7.7	2554a	241a	12619a	5.7	12
9	Banco Popular Español	617	3128	108	30	33	2.5	8	5.0	NA	361	22329	29.7	6
10	Banco Hispano Americano	655	2932	32	17	19	1.5	10	5.8	NA	305	37381	16.0	6
11	Hidroeléctrica Española	853	2253	5	12	14	0.5	13	7.6	3096*	178	13910a*	3.6	12
12	BEX (Banco Exterior Internacional)	936	2070	34	7	9	1.7	16	3.9	NA	124	23901	11.1	6
13	CEPSA	997	1940	22	34	36	1.4	16	3.4	4238a	102a	2077a	8.5	11

SWEDEN

COUNTRY COMPOSITE		68672	46	-3	-2	2.7	21	2.7	99927	3582	240726	14.4		
1	Astra	183	8880	104	16	17	10.3	41	0.5	1522	231	1922	25.2	45
2	Procordia	217	7857	32	28	30	3.5	48	1.5	5983	168	5354	7.3	71
3	L. M. Ericsson	269	6515	32	-22	-21	2.5	13	1.8	7383	509	7619	19.7	34
4	ASEA (4)	NR	6332	96	-24	-23	2.7	15	2.2	21973a	373a	24994a	17.5	34
5	Volvo	441	4277	56	-5	-4	0.8	LOSS	4.5	13440	-164	16496	NEG	42
6	Skanska	515	3774	61	-27	-26	3.0	17	1.7	6013	225a	6038a	17.5	32
7	Stora Kopparbergs Bergslags	553	3517	59	11	12	1.3	17	3.6	10082	205	13628	7.3	23
8	Saab-Scania	605	3170	47	2	3	1.4	14	2.7	4691	232	6971	10.2	38
9	Svenska Handelsbanken	621	3105	20	NA	NA	2.1	10	3.6	NA	320a	44479a	21.4	61
10	Electrolux	633	3065	42	6	7	1.2	11	4.8	13313	288a	10225a	11.0	41
11	Skandinaviska Enskilda Banken	641	3022	11	-13	-12	1.2	11	4.6	NA	268	73237	11.0	61
12	Svenska Cellulosa Aktiebolaget	648	2979	18	-9	-8	2.2	14	2.9	5025	220a	5025a	15.9	23
13	Sandvik	679	2858	53	8	9	1.5	9	2.6	2950	305	3727	16.5	25
14	Alfa-Laval	758	2554	41	0	1	3.0	18	2.3	2889	135	3023	16.5	38
15	AGA	804	2408	50	3	4	2.5	15	2.6	2007	159	2840	16.4	22
16	Skandia	846	2282	30	-10	-9	2.1	50	2.2	2657	46	13428	4.3	63
17	Investor	932	2077	26	-13	-12	4.3	32	2.7	NA	64	1721	13.3	71

SWITZERLAND

COUNTRY COMPOSITE		102199	2775	-8	-4	1.9	24	2.1	114098	5724	479307	9.3		
1	Nestle	43	22026	6065	-4	-1	2.6	14	2.2	31443	1542	24163	17.9	44
2	Roche Holding	80	15251	5297	-4	-1	2.8	34	0.5	6567	642	11735a	8.2	45
3	Sandoz	114	11797	1711	7	11	2.5	19	1.2	8399	656	8706	13.2	45
4	Union Bank of Switzerland	116	11671	2553	1	5	1.0	19	3.6	NA	609	158913	5.3	61
5	Ciba-Geigy	152	9905	2003	-16	-13	1.1	16	2.0	13381	702	17759	6.7	22
6	Swiss Bank Corp.	231	7497	232	2	6	1.0	15	4.1	NA	557	131002	7.0	61
7	Zurich Vers.	319	5637	3294	-1	2	1.5	24	1.4	10655a	262	38920a	6.1	63
8	CS Holding	322	5628	1372	-19	-16	1.3	48	3.7	NA	130	8129*	2.6	61
9	BBC Brown Boveri (4)	NR	5060	3158	-26	-23	2.9	18	1.7	25197	283	26384	15.8	34
10	Schweiz. Ruck.	470	4064	2051	-20	-17	2.4	24	1.5	9981a	187a	28014a	10.2	63
11	Winterthur	533	3662	2784	-3	0	2.4	27	1.7	8475	153	25582a	8.9	63

UNITED STATES

COUNTRY COMPOSITE		2559303	75	15	15	3.9	22	3.1	2681559	150306	5714256	19.1		
1	Exxon	3	72813	58	21	21	2.2	12	4.6	116000	5010	87720	17.8	11
2	General Electric	4	67449	77	12	12	3.1	16	2.6	58400	4300	153800	19.9	34
3	Philip Morris	6	63330	68	62	62	5.3	17	2.5	51200	3540	46570	31.1	43
4	International Business Machines	7	60768	106	-11	-11	1.4	11	4.6	69000	6020	87570	12.8	33
5	Wal-Mart Stores	14	48546	43	52	52	9.1	36	0.4	32602b	1291b	11389b	25.3	54
6	Merck	15	46005	119	44	44	12.0	25	1.9	7672	1781	8030	48.2	45
7	Bristol-Myers Squibb	17	42447	81	32	32	7.8	23	3.0	10300	1748	9215	33.8	45
8	American Telephone & Telegraph	18	40433	37	-14	-14	2.9	15	3.6	37300	2740	43780	19.7	55
9	Coca-Cola	20	38257	57	27	27	10.1	84	1.7	10236	1382	9279	12.0	43
10	Du Pont	22	33156	47	18	18	2.0	14	3.6	40000	2310	38120	14.0	22
11	Johnson & Johnson	25	30181	91	42	42	7.3	23	1.8	11232	1268	7919a	31.7	45
12	Procter & Gamble	28	29489	85	3	3	3.9	17	2.3	24081	1602	18487	22.4	44
13	Mobil	30	26421	66	5	5	1.6	12	4.9	64500	1930	41660	12.7	11
14	General Motors	31	26400	43	-11	-11	0.8	LOSS	3.7	107000	-1990	180300	NEG	42
15	Amoco	32	26165	52	-1	-1	1.9	14	4.2	31600	1910	32210	13.7	11
16	Chevron	35	25915	74	6	6	1.7	12	4.5	38600	2160	35100	15.0	11
17	GTE	36	25908	30	-7	-7	2.2	16	5.3	21393	1714	40750	13.9	55
18	PepsiCo	38	24889	31	27	27	5.0	22	1.5	17803	1091	17143	22.5	43
19	BellSouth	40	24038	50	-11	-11	1.9	15	5.5	14300	1630	30210	12.7	55
20	Abbott Laboratories	42	22732	51	37	37	7.8	22	1.9	6159	966	5563	34.8	45
21	Eli Lilly	45	21237	80	2	2	6.1	19	2.5	5192	1127	7143	31.5	45
22	Minnesota Mining & Mfg.	46	20919	95	15	15	3.4	17	3.3	13021	1308	11079	20.8	71

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	GLOBAL 1000 RANK	MARKET VALUE U. S. \$ MIL.	PRICE PER SHARE U. S. \$	% CHANGE FROM 1990 (U. S. \$) (LOCAL)		PRICE/ BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U. S. \$ MIL.	PROFITS U. S. \$ MIL.	ASSETS U. S. \$ MIL.	RETURN ON EQUITY %	INDUSTRY CODE
Waste Management	50	19974	41	2	2	5.4	27	1.1	6034	709	10518	20.2	52
Atlantic Richfield	51	19665	124	5	5	2.8	12	4.4	18800	1690	23870	23.9	11
Pfizer	53	19466	59	79	79	3.8	24	2.2	6406	801	9052	15.7	45
American International Group	54	19199	91	11	11	1.9	13	0.6	9267	1442	58140	14.9	63
American Home Products	55	18663	59	12	12	6.9	15	3.9	6776	1231	5637	47.4	45
Bell Atlantic	56	18536	47	-10	-10	2.1	14	5.3	12300	1310	28000	14.9	55
Ford Motor	63	17446	37	-20	-20	0.8	LOSS	4.3	97700	1280	173600	NEG	42
Boeing	66	16792	49	-11	-11	2.4	12	2.0	27595	1385	14591	19.9	31
Texaco	68	16651	65	9	9	1.9	12	5.0	41800	1450	25980	16.5	11
Pacific Telesis	70	16288	41	-11	-11	2.2	16	5.3	9716	1030	21580	14.1	55
Ameritech	71	15959	60	-7	-7	2.1	13	5.6	10660	1250	21710	16.0	55
Southwestern Bell	76	15518	52	-11	-11	1.8	14	5.5	9113	1101	22200	12.6	55
Walt Disney	78	15289	116	-10	-10	4.4	20	0.6	5844	824	8023	21.5	53
Schlumberger	79	15270	64	10	10	4.7	26	1.9	5306	570	6176	17.7	36
Anheuser-Busch	82	15083	52	21	21	4.0	17	1.9	10744	842	9634	23.2	43
Dow Chemical	83	14984	56	-11	-11	1.7	10	4.7	19773	1384	23953	17.1	22
US West	87	14461	37	-1	-1	1.6	12	5.7	9957	1199	27050	13.2	55
Nynex	89	14384	72	-18	-18	1.6	13	6.3	13600	1160	26650a	12.5	55
Sears, Roebuck	95	13938	41	12	12	1.1	14	4.9	56000	890	96250	7.8	54
Eastman Kodak	97	13757	42	5	5	2.0	20	4.7	18908	703	24125	10.2	46
Hewlett-Packard	101	13242	54	14	14	2.1	16	0.9	13233	739	11395	12.7	35
Microsoft	107	12687	110	50	50	13.6	34	0.0	1183	279	1105	40.3	52
McDonald's	108	12562	35	1	1	3.6	16	1.1	6776	802	9175a	22.7	53
Federal National Mortgage Assn.	109	12243	51	29	29	4.1	11	2.0	NA	1173	124300a	37.0	62
American Express	112	11902	26	-12	-12	1.9	11	3.6	NA	338	137700	17.9	62
Kellogg	113	11870	98	51	51	6.2	21	2.2	5181	503	3749	29.9	44
Schering-Plough	124	11323	51	8	8	5.4	19	2.6	3223	565	4103	28.1	45
Intel	126	11131	56	16	16	3.1	16	0.0	3921	650	5376	19.0	35
Emerson Electric	127	11110	50	20	20	3.7	18	2.7	7573	613	6376	20.7	34
Pacific Gas & Electric	132	10873	26	13	13	1.4	13	6.3	9470	987	21960	10.9	12
Limited	136	10761	30	19	19	8.7	28	0.9	5254b	398b	2418	31.0	54
J. P. Morgan	144	10280	55	46	46	2.2	12	3.6	NA	775	93100	17.9	61
Campbell Soup	147	10261	79	47	47	6.1	122	1.5	6206	4	4116	5.0	44
Berkshire Hathaway (5)	151	10027	8750	22	22	1.7	22	0.0	2659	394	10670	7.7	71
Marion Merrell Dow	155	9812	36	46	46	7.8	20	2.6	2462	487	2160	40.0	45
K mart	157	9693	49	38	38	1.8	13	3.6	32070b	756b	13899b	14.1	54
H. J. Heinz	158	9665	38	13	13	5.1	19	2.5	6086	504	4487	27.7	44
Warner-Lambert	159	9641	72	17	17	6.8	19	2.5	4687	485	3261	35.9	45
Baxter International	160	9629	35	47	47	2.6	18	2.1	8100	40	8517	14.2	45
General Mills	161	9588	59	46	46	11.8	24	2.2	6448	374	3289	50.0	44
RJR Nabisco Holdings (5)	167	9392	11	NA	NA	2.6	LOSS	0.0	13879	-462	32915	NEG	43
Motorola	170	9371	71	-14	-14	2.4	19	1.1	10885	499	7686a	12.7	35
Sara Lee	173	9300	40	36	36	4.1	20	2.3	11606	470	7636	20.7	44
Westinghouse Electric	174	9270	30	-18	-18	2.2	55	4.7	12915	268	22030	4.0	34
Syntex	178	9036	40	39	39	11.7	22	2.3	1521	342	1787	53.8	45
Toys 'R' Us	180	8989	31	3	3	4.4	29	0.0	5510b	326b	3582b	15.2	54
Union Pacific	188	8786	88	23	23	2.1	14	2.8	6964	618	13078	14.6	57
Dun & Bradstreet	189	8752	49	4	4	4.2	18	4.4	4818	508	4754	23.5	52
Monsanto	193	8609	68	33	33	2.1	18	3.0	8995	515	9236	11.8	22
SCEcorp	194	8602	39	3	3	1.6	11	6.7	7199	786	16310	14.3	12
Southern Co.	196	8562	27	9	9	1.2	14	7.9	7975	604	20090a	9.2	12
Digital Equipment	197	8533	70	-25	-25	1.0	31	0.0	12943	624	11473	3.4	33
American Brands	198	8515	43	28	28	2.3	14	3.6	13781	596	13835	16.8	43
BankAmerica	201	8455	40	29	29	1.5	10	3.0	NA	877	110700	15.3	61
Home Depot	205	8285	66	63	63	11.4	46	0.2	3815b	163b	1640b	24.9	54
General Re	207	8229	94	6	6	2.5	14	1.6	2150	614	11030	18.5	63
MCI Communications	211	8053	32	-26	-26	3.4	34	0.3	7680	299	8249	10.0	55
Upjohn	212	8049	46	18	18	4.5	18	2.5	3033	458	3668	25.7	45
Gillette	215	7919	36	28	28	101.0	21	1.7	4345	368	3114a	472.2	45
International Paper	221	7763	71	35	35	1.4	12	2.4	12960	706	13669	11.7	23
Kimberly-Clark	223	7742	97	37	37	3.4	16	3.1	6407	476	5284	21.2	45
Commonwealth Edison	225	7695	36	15	15	1.2	LOSS	8.3	5262	336	17890	NEG	12
Loews	226	7646	102	-9	-9	1.6	11	1.0	12637	734	32450a	14.0	71
Capital Cities/ABC	227	7592	453	-23	-23	2.3	18	0.0	5386	478	6696	12.5	51
Norfolk Southern	230	7507	48	17	17	1.5	15	3.3	4617	556	10523	10.3	57
Texas Utilities	232	7474	36	0	0	1.0	9	8.2	4543	851	18650	11.5	12
May Department Stores	236	7414	60	5	5	3.2	16	2.7	10035b	500b	7802	19.9	54
Phillips Petroleum	244	7136	28	2	2	2.6	14	4.1	13603	329	12130	18.6	11
Gannett	245	7055	44	8	8	3.4	20	2.8	3441	377	3826	17.0	51
ITT	247	7050	62	8	8	0.9	7	2.8	20604	1056	49040	12.6	71
Time Warner	252	6929	121	14	14	1.1	LOSS	0.8	11517	-227	25337	NEG	51
NCR	256	6819	106	54	54	3.8	20	1.4	6285	369	4547	19.5	33
J. C. Penney	258	6761	58	-12	-12	1.6	15	4.6	17410b	577b	12325b	11.3	54
CPC International	259	6706	89	14	14	4.6	18	2.5	5781	374	4491	25.6	44
Archer Daniels Midland	260	6704	23	-11	-11	1.9	15	0.4	7751	484	5450	12.9	44
Rockwell International	261	6689	28	2	2	1.6	11	3.1	12379	624	9738	14.4	37
USX-Marathon Group (5)	268	6521	26	NA	NA	1.8	13	0.0	13283	508	11931	14.0	11
Cooper Industries	275	6281	57	30	30	2.1	20	2.0	6222	361	7168	10.3	36

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COUNTRY RANK		GLOBAL RANK	MARKET VALUE U.S. \$ MIL.	PRICE PER SHARE U.S. \$	% CHANGE FROM 1990 U.S. \$	PRICE BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL.	PROFITS U.S. \$ MIL.	ASSETS U.S. \$ MIL.	RETURN ON EQUITY %	INDUSTRY CODE
101	Weyerhaeuser	279	6254	30	11	1.6	20	4.0	9024	394	16356	7.9	23
102	Banc One	279	6254	34	15	2.2	14	2.9	NA	423	30340	15.5	61
103	Occidental Petroleum	280	6224	21	-24	1.5	19	4.8	21494	358	19740	7.9	1
104	American Cyanamid	281	1204	65	4	2.7	50	2.3	4570	108	49710	5.2	22
105	ConAgra	281	1204	40	46	5.1	22	1.5	15501	232	4803	23.1	44
106	Aluminum Co. of America	286	6034	8	8	1.2	25	2.3	10710	295	11413	4.7	24
107	Ralston Purina	291	6027	34	21	10.3	16	2.0	7101	396	4395	66.2	44
108	United Telecommunications	291	6027	19	-37	2.7	22	3.4	8345	309	10553	12.1	59
109	Food Lion's	293	5962	18	35	8.5	32	0.8	5584	173	1559	26.2	54
110	Public Service Enterprise Group	297	5926	1	1	1.3	10	7.8	4800	542	14023	12.8	12
111	Unocal	298	590	25	-14	2.3	15	2.8	11808	401	9762	15.6	17
112	Chubb	304	5817	71	48	2.0	11	2.1	3398	522	12270	17.9	63
113	Marsh & McLennan	304	5817	78	-1	5.3	19	3.3	NA	304	2411	28.3	65
114	PPG Industries	306	5817	9	9	2.3	16	3.1	6021	475	8108	14.5	22
115	Corning	306	5817	25	25	3.1	20	1.6	2641	289	3512	15.3	41
116	Albertson's	306	5817	29	29	5.2	24	1.3	8319c	234b	2014b	22.3	54
117	Dayton Hudson	311	5817	80	1	2.6	16	1.8	14739b	410b	8524b	17.6	54
118	United Technologies	311	5679	4	-20	1.1	19	3.8	21783	751	15918	11.6	31
119	Borden	315	5618	38	10	3.1	16	3.0	7633	364	5284	19.7	41
120	Tele-Communications	315	5618	8	8	9.2	LOSS	0.0	3625	-287	12310	NEG	51
121	Duke Power	320	5622	28	1	1.5	11	5.9	3681	538	10083	13.6	12
122	AMP	321	5613	31	1	3.1	20	2.7	3044	287	2929	13.4	35
123	Tenneco	327	5613	40	14	1.7	14	7.0	14511	561	19040	12.0	71
124	Melville	328	5613	10	10	3.0	16	2.6	8687	385	3060	19.5	54
125	Burlington Resources	328	5613	1	-10	1.7	26	1.8	1811	208	6098a	6.7	12
126	American Electric Power	328	5613	29	-1	1.3	11	8.3	5167	496	14500c	11.8	12
127	Raytheon	332	5539	35	35	1.9	10	2.8	9268	557	6119	19.6	31
128	Consolidated Edison of New York	333	5528	24	4	1.2	11	7.7	5739	511	10588	11.2	12
129	Colgate-Palmolive	333	5426	41	28	5.8	18	2.6	5691	321	4158	33.2	44
130	Apple Computer	337	5426	47	13	3.8	11	1.0	5558	475	2976	32.9	33
131	PacificCorp	339	5426	21	-2	1.7	11	7.1	3783	474	12372	14.5	71
132	Citicorp	341	5426	16	-29	0.7	230	6.2	NA	318	217000	0.3	61
133	Humana	341	5398	52	15	3.1	16	2.6	4852	318	3936	18.9	52
134	Xerox	342	5349	38	22	1.1	10	5.2	17973	605	31500	13.1	33
135	Federal Home Loan Mortgage S	344	5321	22	22	2.5	12	2.3	3965	414	40579	20.2	62
136	Rhone-Poulenc Rorer	344	5321	23	23	12.2	292	1.0	2920	1	3832a	4.2	45
137	Caterpillar	344	5222	52	23	1	66	2.3	11103	210	11951	1.7	38
138	Student Loan Marketing Assn.	344	5222	3	3	5.8	17	1.5	NA	301	41120	33.2	62
139	CNA Financial	344	5222	6	6	1.2	13	0.0	9944	367	31090	8.8	63
140	Georgia-Pacific	344	5222	27	27	1.7	19	2.8	12665	365	12060	8.8	23
141	FPL Group	370	4817	31	4	1.6	LOSS	7.9	6289	-391	12953	NEG	12
142	Dominion Resources	379	4800	9	9	1.3	1	7.3	3533	446	10991	11.8	12
143	Wells Fargo	381	4800	93	19	1.7	7	4.2	NA	712	56200	23.0	61
144	UST	381	4800	59	59	10.3	23	2.9	765	223	623	45.4	43
145	Dillard Department Stores S	381	4827	11	41	3.5	26	0.2	3734	183	3008	14.1	54
146	Gap	386	4817	104	104	10.4	29	0.9	1934b	145c	777b	35.2	54
147	Halliburton	389	4793	45	-9	2.1	25	2.2	6920	197	4544	8.4	36
148	NCNB	391	4817	42	9	1.5	13	3.5	NA	300	65280	11.3	61
149	Automatic Data Processing	391	4817	34	10	4.5	21	1.0	1714	210	1090	20.7	52
150	Pitney Bowes	391	4732	1	1	3.0	22	2.3	3196	207	6060	13.4	52
151	Paramount Communications	393	4732	40	-18	1.2	2	1.7	3869	289	6539	5.9	71
152	Houston Industries	394	4732	37	3	1.3	12	8.1	4179	339	11877	11.0	12
153	Electronic Data Systems	403	4643	48	34	2.2	13	1.3	6022	497	NA	NA	52
154	American TV & Communications	407	4643	40	8	1.4	36	0.0	1106	120	2038a	31.5	51
155	Aetna Life & Casualty	407	4624	40	-21	0.6	8	6.7	19021	614	89300	8.0	63
156	CSX	407	4607	47	39	1.3	12	3.0	8205	365	12810	11.0	57
157	Browning-Ferris Industries	411	4514	30	30	3.9	19	2.3	2967	257	3574	20.0	52
158	AMR	414	4417	10	1	LOSS	0.0	11720	-40	13354	NEG	59	
159	Honeywell	414	4417	29	29	2.6	10	2.4	6309	372	4746	20.2	34
160	Entergy	414	4417	24	24	1.1	10	5.0	3982	478	14830	11.1	12
161	Quaker Oats	421	4417	38	13	4.0	20	2.7	5031	229	3326	22.2	44
162	Philadelphia Electric	421	4417	20	23	1.0	16	5.9	3705	106	12560	6.5	12
163	American General	421	4417	18	-18	1.1	8	5.1	4481	562	33810	12.9	63
164	Bankers Trust New York	421	4417	34	24	1.8	7	4.7	NA	665	55000c	24.8	61
165	Amerada Hess	421	4417	14	16	1.4	8	1.1	7081	483	9057	16.7	11
166	McCaw Cellular Communications	421	4417	24	-13	4.3	LOSS	0.0	1008	371	3041a	NEG	55
167	Chemical Waste Management	421	4417	1	-12	4.8	26	1.0	1147	178	1606	17.2	52
168	Allied-Signal	421	4417	30	-18	1	10	6.0	12343	462	10456	11.6	71
169	Central & South West	421	4417	16	16	1.5	15	6.3	2744	386	9074	10.5	12
170	Woolworth	421	4417	0	0	1.8	14	3.2	9789b	317c	4305b	13.6	54
171	Amgen	421	4260	20	249	22.6	157	0.0	381b	34b	308	14.4	45
172	Deere	421	4260	36	-24	1.5	19	3.0	7881	411	9145c	7.8	38
173	Detroit Edison	421	4260	1	1	1.8	9	6.5	3307	515	9950b	20.1	12
174	Rubbermaid	421	4260	35	35	3.5	29	1.1	1534	144	1114	19.2	44
175	Readers Digest Association S	421	4260	31	31	3.6	20	1.7	2010	176	1434	28.0	51
176	Masco	421	4260	27	27	2.3	46	2.1	3209	139	3761	5.0	37
177	Arco Chemical	421	4260	40	1	2.3	15	5.8	2830	308	3739	15.8	22
178	Merrill Lynch	421	4260	13	13	1.4	14	2.4	NA	192	68130	8.9	62
179	Liz Claiborne	421	4260	48	60	7.0	19	0.7	1789	206	849c	35.9	47
180	Novell S	421	4260	1	1	6.3	32	0.0	498	94	494	26.0	33

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	GLOBAL 1000 RANK	MARKET VALUE U.S. \$ MIL.	PRICE PER SHARE U.S. \$	% CHANGE FROM 1990 (U.S. \$) (LOCAL)		PRICE/ BOOK VALUE RATIO	P/E RATIO	YIELD %	SALES U.S. \$ MIL.	PROFITS U.S. \$ MIL.	ASSETS U.S. \$ MIL.	RETURN ON EQUITY %	INDUSTRY CODE
Fluor	476	4030	50	3	3	4.7	30	0.6	7446	139	2476	15.6	38
Walgreen	481	3999	33	39	39	4.2	22	1.4	6047	175	1913	19.5	54
Times Mirror	483	3973	31	-6	-6	2.1	26	3.5	3633	180	4192	8.1	51
Sysco	486	3961	43	25	25	5.1	27	0.7	7591	132	1992	19.2	44
Hershey Foods	487	3957	44	25	25	3.2	20	2.1	2715	196	2078	15.9	44
Air Products & Chemicals	489	3943	71	25	25	2.3	16	2.0	2895	230	3900	14.9	22
Baker Hughes	490	3918	29	-3	-3	2.8	24	1.6	2614	142	2784	11.6	36
Winn-Dixie Stores	495	3887	39	17	17	3.7	18	2.8	9744	153	1733	20.4	54
Salomon	496	3875	35	37	37	1.4	17	1.8	8946	303	109900	8.1	62
Reynolds Metals	499	3860	65	10	10	1.3	11	2.8	6022	391	6527	11.7	24
Newmont Gold	504	3841	37	-17	-17	6.3	29	0.1	643	142	707	21.7	81
UAL	509	3825	154	-1	-1	2.0	LOSS	0.0	11037	94	7994	NEG	56
SunTrust Banks	511	3803	30	28	28	1.7	11	3.1	NA	350	33410	15.2	61
R. R. Donnelley & Sons	512	3796	49	12	12	2.4	18	2.0	3498	226	3343	13.3	52
Nordstrom	514	3780	46	37	37	4.6	29	0.6	2894b	116b	1902b	15.5	54
Coastal	516	3768	36	5	5	1.9	19	1.1	9381	226	9230	10.2	11
Wachovia	523	3722	54	27	27	2.1	12	3.4	NA	297	24050a	17.2	61
Delta Air Lines	524	3722	75	-2	-2	1.3	LOSS	1.6	8582	291	7228	NEG	56
National Medical Enterprises	525	3718	47	31	31	3.0	14	1.7	3935	242	3464	21.0	52
Carolina Power & Light	526	3717	46	5	5	1.6	14	6.6	2617	280	7519	11.7	12
Norwest	527	3716	29	30	30	2.1	10	3.2	NA	281	30630	20.0	61
Cigna	528	3709	52	0	0	0.7	9	5.8	11494a	416	57780a	8.0	63
Primerica	530	3700	32	-3	-3	1.3	9	1.3	NA	373	17960a	14.8	62
Consolidated Natural Gas	534	3658	42	-9	-9	2.0	21	4.4	2715	164	5006	9.4	12
Deluxe	546	3573	43	32	32	5.3	20	2.7	1414	172	924	26.1	52
Ethyl	548	3550	30	0	0	4.0	15	2.0	2514	232	6690	26.0	22
PNC Financial	550	3528	37	4	4	1.4	42	5.8	NA	71	45530	3.2	61
LIN Broadcasting	556	3495	68	-7	-7	5.3	LOSS	0.0	378	-223	675a	NEG	55
Sun	557	3491	33	-18	-18	1.1	15	5.5	13376	229	9000	7.0	11
Illinois Tool Works	559	3480	64	16	16	3.2	19	1.1	2544	182	2150	16.8	38
Sun Microsystems	564	3415	37	21	21	3.7	21	0.0	2466	111	1779	17.2	33
Pennsylvania Power & Light	569	3385	45	6	6	1.5	11	6.9	2389	344	7735	13.6	12
Genuine Parts	570	3377	42	2	2	3.5	16	3.5	3319	207	1352	22.1	37
Chrysler	571	3372	15	-2	-2	0.5	LOSS	4.0	29800	70	46370	NEG	42
Security Pacific	577	3351	27	-32	-32	0.8	134	5.7	NA	161	84730	0.6	61
Scott Paper	581	3314	45	3	3	1.5	28	1.8	5356	148	6901	5.4	45
Alltel (5)	585	3285	42	28	28	3.2	17	3.4	1574	193	2624	18.6	55
Compaq Computer	587	3282	38	-36	-36	1.8	7	0.0	3599	455	2717	24.7	33
Medtronic	598	3223	119	58	58	5.7	28	0.7	866	113	885	20.4	45
Morgan Stanley Group	599	3220	89	25	25	1.7	11	1.7	NA	270	53530	14.7	62
Texas Instruments	601	3198	39	-7	-7	1.7	LOSS	1.8	6567	-39	5048	NEG	35
Genentech	603	3180	29	5	5	3.5	LOSS	0.0	476	-98	1157	NEG	45
Viacom (5)	604	3175	30	11	11	8.8	LOSS	0.0	1600	-90	4028	NEG	51
International Flavors & Fragrances	607	3163	83	23	23	3.5	20	2.9	963	157	1129	18.1	22
Union Camp	610	3152	47	25	25	1.7	16	3.3	2840	230	4400	10.5	23
Costco Wholesale (5)	624	3098	45	118	118	7.2	51	0.0	4133	49	820	14.1	54
Great Lakes Chemical (5)	626	3085	88	51	51	4.1	21	0.6	1066	141	1406	19.2	22
McGraw-Hill	627	3082	63	15	15	3.2	18	3.5	1939	172	2534	17.7	51
Dresser Industries	631	3067	23	-14	-14	1.7	20	2.7	4480	174	3310	8.8	36
Union Electric	635	3064	30	16	16	1.6	11	7.2	2023	294	5760a	14.0	12
Enron	637	3046	60	7	7	1.9	LOSS	4.1	13165	202	9849	NEG	12
Tyson Foods (5)	639	3040	22	31	31	4.2	23	0.2	3825	120	2501	18.4	44
Tribune	640	3039	47	10	10	7.3	LOSS	2.0	2353	-64	2826	NEG	51
W. R. Grace	643	3001	35	23	23	1.6	15	4.0	6754	203	6206	10.6	22
Nike	646	2980	40	1	1	3.8	10	1.4	2235	243	1095	37.2	46
U. S. Surgical (5)	649	2978	61	197	197	12.4	61	0.4	514	46	461	20.4	45
Textron	651	2967	35	43	43	1.1	11	2.9	7918	283	14892	10.3	71
Wheelabrator Technologies	653	2949	27	30	30	4.1	41	0.0	1152	47	2250a	9.9	71
Becton, Dickinson	659	2917	78	15	15	2.5	16	1.5	2013	182	2594	15.3	45
Dow Jones	660	2913	29	5	5	2.0	27	2.6	1720	107	2591	7.4	51
Martin Marietta	662	2908	60	40	40	2.2	9	2.5	6126	328	3611	24.9	31
American Stores	666	2897	84	21	21	2.1	15	1.3	22156b	182b	7245b	14.1	54
NBD Bancorp	667	2891	40	14	14	1.6	11	3.5	NA	275	26750	14.7	61
Rohm & Haas	670	2885	43	27	27	2.3	15	2.9	2824	207	2702	15.7	22
Ohio Edison	676	2861	19	-9	-9	1.1	12	8.0	2226	299	7842	9.1	12
Unocal Exploration (5)	677	2861	11	-38	-38	3.6	17	3.5	913	163	2062	21.2	11
H&R Block (5)	678	2859	54	41	41	6.5	24	2.9	1028	124	942	26.8	62
Torchmark	680	2854	55	14	14	3.0	13	2.9	NA	229	5536	23.3	63
Knight-Ridder	691	2799	56	9	9	3.1	20	2.5	2305	149	2270	15.3	51
Pennzoil	692	2791	69	-6	-6	2.2	33	4.3	2180	94	5261	6.7	11
Geico	695	2780	189	23	23	2.9	14	1.2	1693	208	3576	20.5	63
St. Paul	703	2735	65	11	11	1.2	7	4.0	4005	391	12200	17.2	63
Champion International	706	2731	29	-4	-4	0.7	19	0.7	5090	223	8352	3.7	23
Price	709	2697	56	45	45	4.4	21	0.0	5286	125	1210	20.5	54
Morton International (5)	711	2693	56	31	31	2.5	19	1.7	1639	135	1814	12.9	22
Ingersoll-Rand	713	2690	52	-11	-11	1.7	16	2.5	3738	185	2983	10.8	38
Fleet/Norstar Financial	716	2671	24	6	6	1.4	66	3.3	NA	-74	32510	2.1	61
Burlington Northern	718	2666	35	-6	-6	2.1	17	3.4	4674	222	6075	12.7	57
Medco Containment Services (5)	720	2663	49	110	110	6.3	51	0.1	1004	-8	546	12.3	45

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260	Tandy	722	2661	34	-9	-9	1.5	11	1.8	4500	290	3240	14.3	54
261	Aon	723	2660	41	4	4	1.9	11	3.9	2626	239	9156a	16.6	63
262	Oryx Energy	729	2649	33	-28	-28	4.5	16	3.6	1940	225	5252	27.4	11
263	Lockheed	731	2646	42	18	18	1.1	8	4.8	9958	335	6860	13.8	31
264	U. S. Healthcare (5)	734	2641	38	228	228	11.3	27	0.9	1293	78	613	41.4	45
265	Transamerica	736	2634	35	-12	-12	0.9	12	5.7	NA	253	31780	7.4	62
266	Centel	740	2627	31	-9	-9	2.5	71	2.8	1149	47	3543	3.5	55
267	Dover	742	2624	44	8	8	3.3	18	1.8	2210	156	1468	18.7	21
268	General Public Utilities	750	2589	23	5	5	1.2	9	1.6	2996	278	6916	12.7	12
269	Safeco	752	2587	41	10	10	1.3	9	3.6	1976	278	10560	14.0	63
270	Long Island Lighting	760	2547	23	21	21	1.2	10	6.6	2447	320	8843	12.5	12
271	TRW	761	2545	42	-16	-16	1.3	14	4.3	8169	208	5555	9.7	37
272	Temple Inland	764	2538	47	28	28	1.8	12	1.9	1893	233	7835	14.6	23
273	Travelers	765	2538	25	-19	-19	0.5	LOSS	6.5	12523a	-178	56560a	NEG	63
274	C&S/Sovran	767	2527	19	-29	-29	0.9	19	8.3	NA	229	51230	4.9	61
275	Washington Post	768	2526	213	-17	-17	2.8	17	2.0	1439	175	1497	16.3	51
276	First Interstate Bancorp	770	2518	41	3	3	1.0	7	7.4	NA	439	51360	14.9	61
277	Union Carbide	772	2513	20	0	0	1.1	9	5.0	7621	308	8733	11.4	22
278	Avon Products	773	2511	44	25	25	6.7	15	3.2	3454	195	2059	43.3	45
279	Bausch & Lomb	775	2502	87	37	37	3.0	19	1.7	1369	131	1677	15.6	45
280	First Union (5)	776	2501	23	14	14	1.0	9	4.9	4069	304	40781	10.7	61
281	Newmont Mining	778	2484	37	-20	-20	LOSS	23	1.6	683	101	1302a	NEG	24
282	Wm. Wrigley Jr. (5)	779	2479	63	11	11	6.0	21	2.6	1111	117	564	28.7	44
283	AnnTaylor Stores (5)	781	2478	32	NA	NA	31.6	NM	0.0	417	1	511	1.0	54
284	Baltimore Gas & Electric	787	2459	30	2	2	1.2	18	7.1	2159	213	6711	6.7	12
285	Great Western Financial	788	2458	19	2	2	1.2	13	4.6	NA	193	39410	9.0	61
286	Imcera Group	790	2447	99	63	63	2.8	24	1.0	1425	59	2131	11.3	22
287	Golden West Financial	797	2422	38	20	20	2.0	13	0.5	NA	181	22560	15.3	61
288	Centerior Energy	798	2422	18	-5	-5	0.9	11	8.9	2368	265	11894	7.9	12
289	Gerber Products	801	2413	64	27	27	6.9	21	1.9	1179b	113b	755	32.2	44
290	W. W. Grainger	803	2411	89	21	21	3.0	19	1.4	1935	127	1163	15.3	34
291	Tyco Laboratories	807	2394	51	-4	-4	3.5	18	0.7	2103	119	1417	19.6	71
292	Castle & Cooke (5)	818	2364	40	18	18	2.5	18	1.0	3003	120	2423	13.5	44
293	Hilton Hotels	820	2356	49	-11	-11	2.7	24	2.4	1125	113	2216a	11.3	53
294	National City (5)	829	2328	38	4	4	1.4	11	4.9	2682	234	23743	13.4	61
295	Whirlpool	830	2318	33	12	12	1.6	34	3.3	6623	72	5614	4.7	41
296	Freeport-McMoRan	831	2308	36	10	10	10.9	21	6.9	1581	314	3561a	52.4	26
297	Consolidated Rail	837	2301	57	27	27	0.9	11	2.8	3372	247	7245	7.7	57
298	Brown-Forman (5)	838	2296	84	11	11	3.6	16	2.7	1017	81	1021	22.6	43
299	H. F. Ahmanson	843	2290	20	-7	-7	1.0	13	4.5	NA	191	51200	7.7	61
300	Westvaco	854	2253	35	31	31	1.4	15	3.0	2411	188	3332	9.2	23
301	Phelps Dodge	856	2252	65	11	11	1.3	5	4.6	2636	455	2827	24.9	24
302	Tambrands	858	2248	54	26	26	9.0	23	2.2	632	98	381	40.0	45
303	Wisconsin Energy	863	2231	33	17	17	1.6	12	5.6	1443	187	3361	13.5	12
304	Turner Broadcasting (5)	864	2231	15	-13	-13	NEG	LOSS	0.0	1394	-16	2153	NEG	51
305	Pacific Enterprises	865	2227	32	-27	-27	1.3	11	11.0	6923	232	7291	12.6	12
306	Chase Manhattan	866	2220	19	-27	-27	0.6	LOSS	6.2	NA	-334	107400a	NEG	61
307	Freeport-McMoRan Copper & Gold (5)	867	2208	24	81	81	10.4	21	5.4	434	93	675	48.4	81
308	Clorox	869	2202	41	-4	-4	2.7	18	3.8	1484	154	1138	15.2	44
309	Northeast Utilities	871	2201	20	4	4	1.3	10	8.7	2616	211	6523a	12.1	12
310	Sherwin-Williams	875	2190	25	34	34	2.9	18	1.7	2267	123	1504	15.7	22
311	Potomac Electric Power	876	2189	21	-1	-1	1.5	13	7.4	1412	170	5240	11.2	12
312	Capital Holding	881	2178	49	3	3	1.6	14	2.5	1171	166	16670	10.8	63
313	CMS Energy	884	2167	27	-9	-9	1.1	LOSS	1.8	2980	-494	8604a	NEG	12
314	Republic New York	886	2164	63	29	29	1.6	11	2.2	NA	201	29600	14.0	61
315	CBS	887	2158	164	-19	-19	1.6	210	0.6	3261	112	4692	0.8	51
316	Coca-Cola Enterprises	888	2156	19	17	17	1.6	28	2.7	4034	93	5021	5.9	43
317	Bank of New York	890	2155	31	-17	-17	0.9	20	4.9	NA	308	48860a	4.5	61
318	CoreStates Financial	893	2152	40	-7	-7	1.6	21	4.8	NA	114	23520	7.5	61
319	Lincoln National	894	2151	49	-11	-11	1.0	12	5.6	8490	191	27600	7.9	63
320	Amex	895	2145	25	2	2	1.0	10	3.2	3788	226	4920	9.3	24
321	Mead	896	2142	37	12	12	1.4	30	2.7	4772	106	3889	4.6	23
322	United Artists Entertainment	897	2142	15	-1	-1	1.5	LOSS	0.0	1460	-159	4077a	NEG	51
323	Circus Circus Enterprises (5)	898	2141	78	24	24	11.6	26	0.0	692	76	792	45.2	53
324	Federal Express	904	2132	40	-13	-13	1.3	118	0.0	7015	116	5675	1.1	52
325	Arkla	905	2129	19	-19	-19	2.8	17	5.8	2436	106	3886a	16.0	12
326	Contel Cellular (5)	909	2123	21	13	13	77.1	LOSS	0.0	167	-103	1665	NEG	55
327	Northern States Power	913	2119	34	-5	-5	1.4	12	6.8	2065	193	4762	11.4	12
328	James River Corp. of Virginia	914	2115	26	3	3	1.0	LOSS	2.3	3391c	10	5741	NEG	23
329	Newell (5)	917	2111	35	21	21	4.0	22	1.7	1073	101	871	18.2	41
330	Marriott	918	2106	23	-8	-8	5.2	18	1.2	7646	144	6926	28.5	53
331	Alza	919	2105	65	59	59	9.6	87	0.0	109	25	531	11.1	45
332	National Health Laboratories (5)	920	2105	21	63	63	8.2	24	0.6	502	83	374	34.0	45
333	Allegheny Power System	921	2105	40	2	2	1.3	11	8.0	2298	191	4561	11.5	12
334	Crown Cork & Seal	922	2102	73	19	19	2.2	19	0.0	3072	107	2597	11.4	26
335	Super Valu Stores	924	2093	28	1	1	2.4	14	2.4	11612b	155b	2429	17.8	54
336	St. Jude Medical (5)	926	2082	44	37	37	7.6	31	0.0	175	65	278	24.4	45
337	U. S. Bancorp (5)	928	2081	35	42	42	1.6	11	2.9	1920	183	17613	14.4	61
338	US West New Vector Group (5)	929	2079	41	14	14	14.2	LOSS	0.0	274	-4	511	NEG	55
339	UNUM (5)	931	2077	62	28	28	1.7	11	1.7	2170	185	9514	15.1	63

Footnotes on page 57

THE GLOBAL 1000

	GLOBAL 1000 RANK	MARKET VALUE U.S. \$ MIL.	PRICE PER SHARE U.S. \$	% CHANGE FROM 1990 (U.S. \$) (LOCAL)		PRICE/ BOOK VALUE RATIO	P:E RATIO	YIELD %	SALES U.S. \$ MIL.	PROFITS U.S. \$ MIL.	ASSETS U.S. \$ MIL.	RETURN ON EQUITY %	INDUSTRY CODE
Roadway Services	933	2075	54	41	41	2.7	17	2.0	2971	119	1341	15.4	57
Kerr-McGee	935	2071	43	12	-12	1.4	18	3.6	3683	113	3473	7.6	11
Sigma-Aldrich (5)	940	2062	42	26	26	5.4	28	0.5	529	71	546	19.4	45
Niagara Mohawk Power	942	2059	15	9	9	1.1	35	0.0	3155	83	7770	3.0	12
Florida Progress (5)	943	2055	40	9	9	1.4	11	6.9	2011	197	5046	13.0	12
Chiquita Brands International (5)	946	2052	45	96	96	2.8	20	1.3	4273	94	2174	14.1	44
Eaton	951	2038	60	-2	-2	1.8	16	3.7	3639	169	3013	11.1	37
McDonnell Douglas	957	2026	53	17	17	0.6	9	2.6	16246	176	14960	6.6	31
Columbia Gas System	958	2025	40	-13	-13	1.3	18	5.8	2358	105	6197	6.9	12
Nalco Chemical	959	2025	58	7	7	4.5	17	2.9	1212	131	1037	27.0	22
Reebok International	962	2016	23	19	19	2.6	14	1.3	2160	177	1403	18.3	46
Rite Aid	967	1992	43	26	26	2.6	17	2.3	3447b	107b	1539	15.7	54
Beneficial	968	1990	61	17	17	1.7	12	4.3	NA	117	7948a	14.5	62
Fund American	971	1986	64	102	102	1.8	48	1.1	275	129	11720a	3.7	63
Southern New England Telecomms.	974	1983	33	-7	-7	1.7	16	5.4	1620	127	3178a	10.6	55
Teco Energy (5)	977	1976	35	21	21	2.4	14	5.0	1097	143	2513	16.5	12
Pet	987	1956	19	NA	NA	4.2	68	1.3	1863	30	1521	6.1	44
Chemical Banking (5)	989	1954	21	-22	-22	0.7	13	4.7	7697	291	73019	4.9	61
Lyondell Petrochemical (5)	991	1950	24	30	30	18.6	5	7.4	6495	356	1372	358.9	22
Fifth Third Bancorp (5)	995	1942	49	56	56	2.4	16	2.2	834	120	7956	15.6	61

OTHER MARKETS AROUND THE WORLD

The Global 1000 ranking excludes companies from countries where stock markets are largely closed to foreign investors and where major corporations are often privately owned. Many of

these companies are significant global competitors, and the list below includes those companies where annual revenues for the most recent fiscal year are over \$1 billion.

Company	Sales U.S. \$ Bil.	Profits U.S. \$ Mil.	Company	Sales U.S. \$ Bil.	Profits U.S. \$ Mil.	Company	Sales U.S. \$ Bil.	Profits U.S. \$ Mil.
SOUTH KOREA			DAELIM INDUSTRIAL	1.7	14	NAN YA PLASTICS	2.0	173
DAEWOO (Trading)	11.1	17	COMMERCIAL BANK OF KOREA	1.5	90	FIRST COMMERCIAL BANK	2.0	200
DAI (Trading)	8.8	10	KOREA FIRST BANK	1.4	117	HUA NAN COMMERCIAL BANK	2.0	210
DO (Trading)	7.3	81	HANIL BANK	1.4	122	CHANG HWA COMMERCIAL BANK	1.9	210
ELECTRIC POWER	7.0	846	CHOHUNG BANK	1.4	103	FORMOSA PLASTICS	1.1	150
IRON & STEEL	6.7	110	DONG-AH CONST.	1.3	14	EVERGREEN MARINE (TAIWAN)	1.0	38
DAI MOTOR	6.5	94	DAEWOO HEAVY INDUSTRIES	1.3	23	TATUNG	1.0	8
ING ELECTRONICS	6.3	102	CHEIL FOODS & CHEMICAL	1.2	11	FORMOSA CHEMICALS & FIBER	1.0	156
ING	4.4	44	ASIA MOTORS	1.2	18	MEXICO		
GOLDSTAR INTERNATIONAL	4.2	6	HYUNDAI PRECISION INDUSTRIES	1.2	24	TELEFONOS DE MEXICO	3.9	1,140
TAR	4.2	47	BANK OF SEOUL	1.2	74	GRUPO VITRO	2.8	252
MOTORS	3.5	59	SSANGYONG OIL REFINING	1.1	36	GRUPO INDUSTRIAL ALFA	2.2	191
DAI MOTOR SERVICE	2.9	45	KOLON INTERNATIONAL	1.1	12	CIFRA	2.2	154
YONG (Trading)	2.8	15	SAMSUNG ENG. & CONST.	1.1	34	GRUPO VISA	1.7	107
DAI ENG. & CONST.	2.8	24	HANYANG CHEMICAL	1.0	31	GRUPO DESC	1.5	74
YONG (Trading)	2.4	11	SSANGYONG CEMENT	1.0	42	CEMENTOS MEXICANOS	1.3	148
IN AIR	2.3	-11	GOLDSTAR CABLE	1.0	28	BRAZIL†		
(Petrochemicals)	2.2	86	SAMSUNG ELECTRON DEVICES	1.0	42	PAO DE ACUCAR	2.5	62
DO ELECTRONICS	1.8	18	TAIWAN			VOTORANTIM	2.3	92
ING (Trading)	1.8	1	CATHAY LIFE INSURANCE	4.2	175	PETROLEO IPIRANGA	1.9	13
			CHINA STEEL	2.2	562			

DATA: DAEWOO SECURITIES CO., COMPANY REPORTS, BW

† Fiscal 1989

KEY TO INDUSTRY CODES

Left-hand digit represents broad economic sector as defined by Morgan Stanley Capital International. Right-hand digit is industry classification code within each economic sector.

ENERGY

- 11. Energy sources
- 12. Utilities-electrical & gas

MATERIALS

- 21. Building materials & components
- 22. Chemicals
- 23. Forest products & paper
- 24. Metals-nonferrous
- 25. Metals-steel
- 26. Misc. materials & commodities

CAPITAL EQUIPMENT

- 31. Aerospace & military technology
- 32. Construction & housing

- 33. Data processing & reproduction
- 34. Electrical & electronics
- 35. Electronic components & instruments
- 36. Energy equipment & services
- 37. Industrial components
- 38. Machinery & engineering

4. CONSUMER GOODS

- 41. Appliances & household durables
- 42. Automobiles
- 43. Beverages & tobacco
- 44. Food & household products
- 45. Health & personal care
- 46. Recreation, other consumer goods
- 47. Textiles & apparel

5. SERVICES

- 51. Broadcasting & publishing
- 52. Business & public services
- 53. Leisure & tourism
- 54. Merchandising
- 55. Telecommunications
- 56. Transportation-airlines
- 57. Transportation-road & rail
- 58. Transportation-shipping
- 59. Wholesale & international trade

6. FINANCE

- 61. Banking
- 62. Financial services
- 63. Insurance
- 64. Real estate

7. OTHER

- 71. Multi-industry
- 81. Gold mines

THE GLOBAL 1000

ALPHABETICAL LIST OF COMPANIES

The number preceding each company is its Global 1000 rank. The code following each company shows its nationality and rank within that nation. To find the statistics for a company, turn to the country listing and look for the company by its rank.

A

- 835 Aachener & Munchener Bet (GE-35)
122 ABB (Switzerland) (CH-20)
273 ABB (Switzerland) (CH-20)
42 ABB (Switzerland) (CH-20)
366 ABB (Switzerland) (CH-20)
684 ABB (Switzerland) (CH-20)
746 ABB (Switzerland) (CH-20)
952 AEG (GE-38)
741 AEG (GE-38)
809 AEG (GE-38)
804 AEG (GE-38)
843 AEG (GE-38)
955 AEG (GE-38)
286 AEG (GE-38)
489 Air Products & Chemicals (US-186)
834 Air Products & Chemicals (US-186)
238 Air Products & Chemicals (US-186)
748 Air Products & Chemicals (US-186)
312 Albertson's (US-116)
392 Alcan Aluminum (CA-10)
128 Alcatel Alsthom (FR-2)
95 Alcatel Cable (FR-37)
758 Alcatel Cable (FR-37)
111 All Nippon Airways (JA-30)
413 Allianz (DE-15)
921 Allegheny Power System (US-333)
33 Allianz Holding (GE-1)
213 Allied-Lyons (BR-24)
438 Allied-Signal (US-168)
585 Alltel (US-217)
941 Alps Electric (JA-292)
288 Aluminum Co. of America (US-106)
919 Alza (US-111)
826 Amada (JA-262)
985 Amas (US-320)
986 Amara (US-15)
312 Amerasia Hess (US-165)
683 American Bank Resources (CA-19)
198 American Brands (US-75)
281 American Cyanamid (US-104)
331 American Electric Power (US-126)
112 American Express (US-47)
228 American General (US-163)
55 American Home Products (US-27)
54 American International Group (US-26)
666 American Stores (US-242)
18 American Telephone & Telegraph (US-8)
407 American TV & Communs (US-154)
71 Ameritech (US-33)
443 Amgen (US-171)
32 Amoco (US-15)
426 AMP (US-122)
414 AMR (US-158)
228 Anglo American (SA-2)
112 Anheuser Busch (US-37)
781 AnnTaylor Stores (US-283)
700 ANZ Group Holdings (AS-10)
796 Aoki (JA-254)
723 Aon (US-261)
337 Apple Computer (US-130)
747 Arabian Oil (JA-232)
260 Archer Daniels Midland (US-97)
464 Arco Chemical (US-177)
330 Argyle Group (BR-32)
905 Arkio (US-325)
445 Asahi Breweries (JA-143)
219 Asahi Chemical Industry (JA-78)
117 Asahi Glass (JA-45)
828 ASDA Group (BR-75)
NR ASEA (SWE-4)
343 Ashikaga Bank (JA-115)
69 Assicurazioni Generali (IT-1)
471 Associated British Foods (BR-42)
183 Astra (SWE-1)
51 Atlantic Richfield (US-24)
393 Automatic Data Processing (US-149)
773 Avon Products (US-278)
361 Avon Products (US-278)

B

- 531 BAA (BR-52)
490 Baker Hughes (US-127)
787 Baltimore Gas & Light (US-284)
279 Banc One (US-102)
501 Banca Commerciale Italiana (IT-1)
805 Banca Ambrosiana (IT-1)
234 Banco Bilbao Vizcaya (SP-2)
416 Banco Central (SP-6)
301 Banco de Santander (SP-4)
701 Banco di Roma (IT-12)
513 Banco Espanol de Credito (SP-7)
655 Banco Hispano Americano (SP-10)
617 Banco Popular Espanol (SP-9)
385 Bank of Fukuoka (JA-129)
463 Bank of Hiroshima (JA-152)
608 Bank of Kyoto (JA-195)
521 Bank of Montreal (CA-12)
890 Bank of New York (US-317)
630 Bank of Nova Scotia (CA-18)
944 Bank of Scotland (BR-88)
49 Bank of Tokyo (JA-19)
140 Bank of Yokohama (JA-56)
201 BankAmerica (US-76)
429 Bankers Trust New York (US-164)

B

- 786 Banyu Pharmaceutical (JA-251)
111 Barclays Bank (BR-12)
195 BASF (GE-10)
242 Bass (BR-26)
62 B. A. T. Industries (BR-7)
775 Bausch & Lomb (US-279)
160 Baxter International (US-61)
133 Bayer (GE-5)
541 Bayerische Hypotheken (GE-23)
529 Bayerische Vereinsbank (GE-22)
NR BBC Brown Boveri (SWE-9)
123 BCE (Bell Canada Enterprises) (CA-1)
659 Becton, Dickinson (US-239)
56 Bell Atlantic (US-28)
40 BellSouth (US-19)
968 Beneficial (US-352)
151 Berkshire Hathaway (US-56)
847 BET (BR-76)
936 BEX (SP-12)
937 BICC (BR-87)
678 Black (HBR) (US-247)
855 Blue Circle Industries (BR-77)
350 BMW (GE-14)
693 BNP (FR-29)
432 BOC Group (BR-39)
66 Boeing (US-30)
274 Boots (BR-29)
811 Boral (AS-13)
315 Borden (US-119)
744 Brabrand Industries (AS-11)
299 Bridgestone (JA-106)
17 Bristol-Myers Squibb (US-7)
739 British Aerospace (BR-85)
908 British Airways (BR-15)
57 British Gas (BR-5)
24 British Petroleum (BR-2)
435 British Steel (BR-40)
19 British Telecommunications (BR-1)
91 Broken Hill Proprietary (AS-1)
412 Browning-Ferris Industries (US-157)
818 Brown-Forman (US-298)
192 BSH (FR-5)
119 BTR (FR-14)
355 BTR Nylas (AS-4)
718 Burlington Northern (US-258)
329 Burlington Resources (US-125)

C

- 767 C&S/Sovran (US-274)
171 Cable & Wireless (BR-18)
437 Cadbury Schweppes (BR-41)
147 Campbell Soup (US-55)
360 Canadian Imperial Bank (CA-8)
316 Canadian Pacific (CA-7)
573 Canal Plus (FR-21)
208 Canon (JA-75)
839 Canon Sales (JA-268)
980 Cap Gemini Societe (FR-40)
227 Capital Cities/ABC (US-86)
881 Capital Holding (US-312)
705 Carlsberg (DE-3)
526 Carolina Power & Light (US-200)
433 Carrefour (FR-17)
726 Casio Computer (JA-224)
818 Castile & Cooke (US-292)
352 Caterpillar (US-137)
613 Cathay Pacific Airways (HK-9)
887 CBS (US-315)
740 Centel (US-266)
798 Centor Energy (US-288)
439 Central & South West (US-169)
997 CEPSA (SP-13)
706 Champion International (US-253)
866 Chase Manhattan (US-306)
989 Chemical Banking (US-357)
436 Chemical Waste Management (US-167)
375 Cheung Kong Holdings (HK-4)
35 Chevron (US-16)
255 Chiba Bank (JA-92)
416 China Light & Power (HK-5)
948 Chiquita Brands International (US-345)
517 Chiyoda Corp. (JA-168)
874 Chiyoda Fire & Marine (JA-280)
571 Chrysler (US-214)
304 Chubb (US-112)
72 Chubu Electric Power (JA-24)
912 Chugan Pharmaceutical (JA-287)
735 Chugoku Bank (JA-229)
253 Chugoku Electric Power (JA-90)
152 Ciba-Geigy (SWE-5)
528 Cigna (US-202)
898 Circus Circus Enterprises (US-323)
340 Citicorp (US-132)
833 Citizen Watch (JA-265)
869 Clorox (US-308)
979 CMB Packaging (FR-39)
884 CMS Energy (US-313)
370 CNA Financial (US-139)
516 Coastal (US-196)
20 Coca-Cola (US-9)
888 Coca-Cola Enterprises (US-316)
421 Coles Myer (AS-5)
335 Colgate-Palmolive (US-129)
958 Columbia Gas System (US-348)
535 Commercial Union Assurance (BR-54)
482 Commerzbank (GE-20)

C

- 225 Commonwealth Edison (US-84)
960 Compagnie Bancaire (FR-38)
587 Compaq Computer (US-218)
285 Conagra (US-105)
333 Consolidated Edison of N. Y. (US-128)
534 Consolidated Natural Gas (US-204)
837 Consolidated Rail (US-297)
909 Contel Cellular (US-326)
275 Cooper Industries (US-100)
893 CoreStates Financial (US-318)
310 Corning (US-115)
565 Cosmo Oil (JA-182)
624 Costco Wholesale (US-226)
499 Courtauld's (BR-67)
329 CPC International (US-96)
321 CRA (AS-3)
925 Credit Foncier de France (FR-36)
668 Credit Lyonnais (FR-72)
656 Creditanstalt-Bankverein (AT-1)
597 Credito Italiano (IT-9)
922 Crown Cork & Seal (US-334)
322 CS Holding (SWE-8)
799 CSK (JA-255)
580 CSR (AS-8)
410 CSX (US-156)

D

- 190 Dai Nippon Printing (JA-69)
999 Daicel Chemical Industries (JA-308)
868 Daicel Steel (JA-278)
506 Daiei (JA-167)
809 Daifuku (JA-282)
460 Daiichi Pharmaceutical (JA-150)
584 Daikin Industries (JA-187)
755 Daikyo Kanko (JA-238)
48 Daimler-Benz (GE-2)
615 Damppan Ink & Chemicals (JA-197)
819 Danippon Pharmaceutical (JA-259)
412 Dairy Farm Intl. Holdings (HK-14)
346 Datsunwa Corp. (JA-117)
96 Daewa Bank (JA-35)
257 Daewa House Industry (JA-93)
102 Daewa Securities (JA-39)
10 Da-ichi Kogyo Bank (JA-5)
636 Da-ichi Kogyo Fire & Marine (JA-203)
612 Dampskibsselskabet AF 1912 (DE-1)
199 Dampskibsselskabet Svendborg (DE-2)
313 Dayton Hudson (US-117)
182 De Beers Centenary (SA-1)
446 Deere (US-172)
861 Delhaize Le Lion (BE-6)
524 Delta Air Lines (US-198)
468 Deluxo (US-205)
707 Den Danske Bank (DE-4)
494 Detroit Edison (US-173)
64 Deutsche Bank (GE-4)
850 Deutsche Lufthansa (GE-36)
547 Development Bank of Singapore (SI-2)
197 Digital Equipment (US-74)
386 Dillard Department Stores (US-145)
78 Disney (Walt) (US-35)
579 Dominion Resources (US-142)
312 Donnelley (R. R.) & Sons (US-194)
763 Dortsche Petroleum (NE-11)
742 Dover (US-267)
83 Dow Chemical (US-348)
660 Dow Jones (US-200)
218 Dresdner Bank (GE-11)
631 Dresser Industries (US-229)
813 Driehofen Consolidated (SA-4)
953 DSM (NE-12)
22 Du Pont (US-10)
323 Duke Power (US-121)
189 Dun & Broadstreet (US-70)

E

- 817 EA-Generali (AT-2)
97 Eastman Kodak (US-42)
951 Eaton (US-346)
572 Ebara (JA-184)
623 Eisai (JA-200)
270 Electrabel (BE-7)
872 Electrafina (BE-7)
633 Electrolux (SWE-10)
405 Electronic Data Systems (US-153)
74 Elf Aquitaine (FR-1)
671 Elsevier (NE-7)
127 Elsevier Electric (US-51)
324 Endesa (SP-5)
627 Enron (US-231)
420 Entergy (US-160)
485 Enterprise Oil (BR-45)
269 Encison (L. M.) (SWE-3)
548 Ethyl (US-206)
594 Euro Tunnel (FR-18)
430 Eurotunnel (FR/BR-NP)
NR Eurotunnel (London) (BR-82)
NR Eurotunnel (Paris) (FR-35)
3 Exxon (US-1)

F

- 165 Fancu (JA-64)
904 Federal Express (US-324)
344 Federal Home Loan Mortgage (US-135)
109 Federal National Mortgage Assn. (US-46)
822 Ferruzzi Finanziaria (IT-14)

F

- 153 Fiat Group (IT-2)
995 Fifth Third Bancorp (US-359)
770 First Interstate Bancorp (US-276)
776 First Union (US-280)
309 Fisons (BR-31)
716 Fleet/Norstar Financial (US-257)
652 Fletcher Challenge (NZ-1)
943 Florida Progress (US-344)
476 Fluor (US-181)
685 Fondiaria (It) (IT-11)
295 Food Lion (US-109)
63 Ford Motor (US-29)
747 Fosters Brewing Group (AS-12)
376 FPL Group (US-141)
831 Freeport-McMoRan (US-296)
867 Freeport-McM. Copper & Gold (US-307)
8 Fuji Bank (JA-3)
395 Fuji Electric (JA-130)
880 Fuji Heavy Industries (JA-281)
120 Fuji Photo Film (JA-46)
737 Fujikura (JA-230)
452 Fujisawa Pharmaceutical (JA-145)
957 Fujitsu Corp. (JA-148)
915 Fujitsu Tourist Enterprises (JA-288)
84 Fujitsu (JA-28)
840 Fukuko City Bank (JA-269)
717 Fukuyama Transporting (JA-221)
971 Fund America (US-353)
500 Furukawa Electric (JA-163)

G

- 245 Gannett (US-91)
388 Gap (US-146)
695 Geico (US-251)
667 Gencor (SA-3)
603 Genentech (US-222)
748 General Accident Fire & Life (BR-44)
179 General Electric (BR-19)
4 General Electric (US-2)
161 General Mills (US-62)
31 General Motors (US-14)
750 General Public Utilities (US-268)
207 General Re (US-78)
938 Generale des Eaux (BE-9)
184 Generale des Eaux (Compagnie) (FR-4)
571 Genie Partners (US-213)
370 Georgia-Pacific (US-140)
801 Gerber Products (US-289)
215 Gillette (US-81)
26 Glaxo Holdings (BR-3)
903 Gold Fields of South Africa (SA-5)
797 Golden West Financial (US-287)
643 Grace (W. R.) (US-234)
803 Grainger (W. W.) (US-290)
104 Grand Metropolitan (BR-11)
626 Great Lakes Chemical (US-227)
348 Great Universal Stores (BR-33)
788 Great Western Financial (US-285)
906 Groupe Bruxelles Lambert (BE-8)
664 Groupe Victoire (FR-26)
3 GTE (US-15)
647 Guardian Royal Exchange (BR-63)
85 Guinness (BR-10)
451 Gunma Bank (JA-144)

H

- 367 Hachijuni Bank (JA-125)
389 Halliburton (US-147)
416 Hang Seng Bank (HK-7)
458 Hankyu Corp. (JA-149)
61 Hanson Trust (BR-6)
248 Hanwa (JA-86)
663 Hasegawa Kumeten (JA-206)
595 Havas (FR-22)
844 Hazama (JA-271)
763 Heidelberg Cement (GE-39)
724 Heineken (NE-8)
158 Heinz (H. J.) (US-59)
877 Henderson Land Development (HK-15)
373 Henkel (GE-16)
487 Hershey Foods (US-185)
101 Hewlett-Packard (US-43)
853 Hidroelectrica Espanola (SP-11)
813 Hilldown Holdings (BR-83)
928 Hilton Hotels (US-293)
757 Hino Motors (JA-239)
601 Hitachi Cable (JA-192)
29 Hitachi Ltd. (JA-13)
591 Hitachi Metals (JA-190)
365 Hitachi Zosen (JA-124)
423 Hochtief (GE-17)
172 Hoechst (GE-9)
998 Hokkaido Bank (JA-307)
468 Hokkaido Electric Power (JA-153)
264 Hokkaido Takushoku Bank (JA-95)
296 Hokuriku Bank (JA-105)
442 Hokuriku Electric Power (JA-141)
771 Holzmann (Philipp) (GE-31)
205 Home Depot (US-77)
163 Honda Motor (JA-62)
415 Honeywell (US-159)
156 Hong Kong Telecommunications (HK-1)
629 Hongkong Electric Holdings (HK-10)
694 Hongkong Land Holdings (HK-11)
690 Honshu Paper (JA-217)
397 Houston Industries (US-152)

H

- 334 HSBC Holdings (HK-3)
341 Humana (US-133)
293 Hutchison-Whampoa (HK-2)
566 Hyogo Bank (JA-183)
592 Iberdruero (SP-8)
559 Illinois Tool Works (US-210)
579 Imasco (CA-14)
790 Imcera Group (US-286)
73 Imperial Chemical Industries (BR-9)
177 Imperial Oil (CA-4)
948 Inax (JA-293)
910 Inchope (BR-86)
536 Inco (CA-13)
5 Industrial Bank of Japan (JA-2)
713 Ingersoll-Rand (US-256)
126 Intel (US-50)
7 International Business Machines (US-224)
607 Intl. Flavors & Fragrances (US-224)
221 International Paper (US-82)
282 Internationale Nederlanden Group (NL-1)
932 Investor (SWE-17)
806 Istar-Amperwerke (GE-33)
400 Isetan (JA-133)
251 Ishikawajima-Harima Heavy Inds. (JA-10)
503 Isuzu Motors (JA-165)
930 Italcementi (IT-17)
243 Itoh (C.) (JA-84)
105 Ito-Yokado (JA-41)
247 IIT (US-92)

J

- 914 James River Corp. of Virginia (US-35)
93 Japan Air Lines (JA-33)
785 Japan Radio (JA-250)
825 Japan Steel Works (JA-261)
702 Jardine Matheson Holdings (HK-12)
927 Johannesburg Consolidated (SA-6)
25 Johnson & Johnson (US-11)
292 Joyo Bank (JA-103)
782 Jujo Paper (JA-247)
540 Jusco (JA-172)

K

- 157 K mart (US-58)
143 Kajima (JA-52)
916 Kakusai Electric (JA-297)
749 Kankendo (JA-235)
899 Kanebo (JA-283)
696 Kankaku Securities (JA-218)
47 Kansai Electric Power (JA-18)
364 Kao (JA-123)
721 Karlstad (GE-28)
721 Kaufhof (GE-30)
294 Kawasaki Heavy Industries (JA-104)
792 Kawasaki Kisen (JA-252)
141 Kawasaki Steel (JA-57)
303 KDD (JA-108)
558 Keihin Electric Express Railway (JA-45)
455 Keio Teito Electric Rail (JA-147)
620 Keisei Electric Railway (JA-198)
113 Kellogg (US-48)
935 Kerr-McGee (US-341)
223 Kimberly-Clark (US-83)
586 Kinden (JA-188)
519 Kingfisher (BR-50)
129 Kinki Nippon Railway (JA-66)
161 Kinn Brewery (JA-47)
691 Knight-Ridder (US-249)
129 Kobe Steel (JA-49)
622 Koito Mfg. (JA-199)
590 Kokuyo (JA-189)
271 Komatsu (JA-98)
698 Konica (JA-220)
224 Kubota (JA-80)
724 Kumagai Gumi (JA-155)
964 Kurama Industries (JA-298)
665 Kuraray (JA-207)
191 Kyocera (JA-70)
474 Kyowa Hako (JA-156)
44 Kyowa Saitama Bank (JA-17)
164 Kyushu Electric Power (JA-63)
488 Kyushu Matsushita Electric (JA-159)

L

- 508 Ladbroke Group (BR-48)
555 Lafarge Copper (FR-19)
708 Ladlow (CA-21)
424 Land Securities (BR-38)
981 Lasmo (BR-91)
151 Legal & General Group (BR-58)
815 Leont Leont (AS-14)
45 Lilly (EL) (US-21)
136 Limited (US-53)
556 Lin Broadcast (US-208)
894 Lincoln National (US-319)
576 Linde (GE-24)
466 Luz Claiborne (US-179)
466 Lloyds Abbey Life (BR-37)
235 Lloyds Bank (BR-25)
731 Lockheed (US-263)
266 Loews (US-85)
720 Long Island Lighting (US-270)
27 Long-Term Credit Bank of Japan (JA-70)
730 Lonrho (BR-70)

How do you plan to keep that's moving so fast?

If you are responsible for guiding a major corporation through the 1990s, it must seem that new concerns are being added to your management agenda almost daily.

The established concepts of what a corporation is and what it stands for, how it views its product mix, where and how it produces what it sells, where it sees its market opportunities, who it views as partners and competitors, how it finances its present and future growth, how best it can work within governmental regulations and policies—all these once-familiar parameters are changing with astonishing, if not alarming, speed.

All this must seem especially true if your interests are international in scope.

Dates such as 1992 and 1997 foretell of major changes in long-established routines of managing the forces of economics, protectionism, finance and politics.

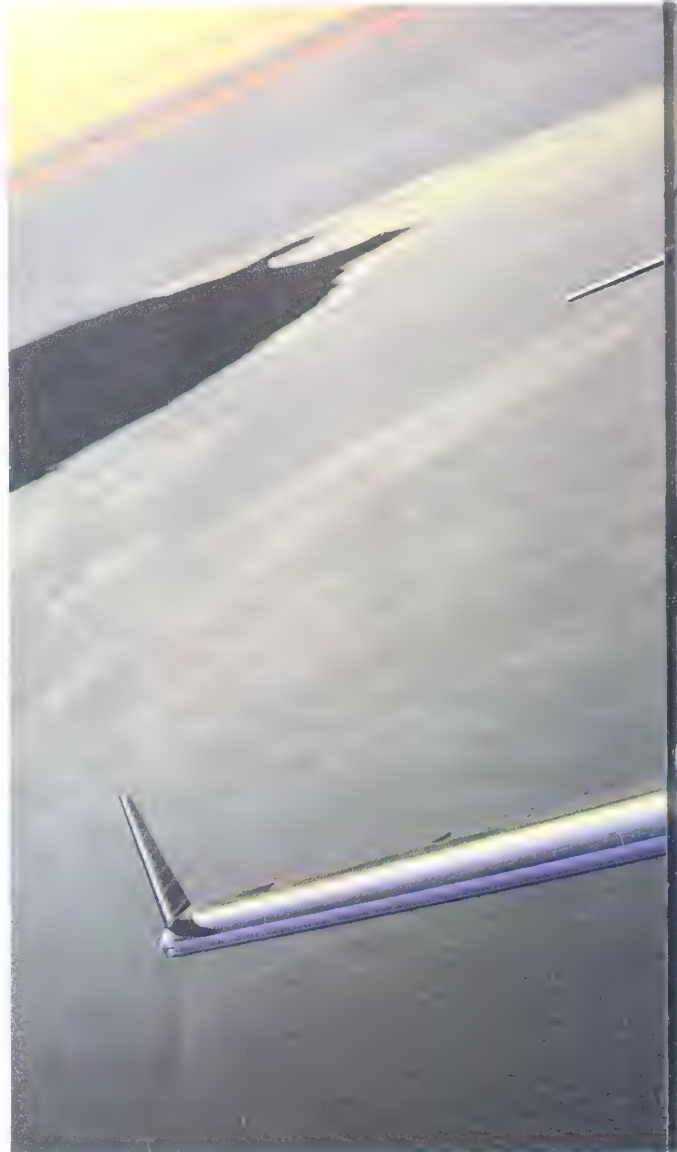
The words "Pacific Rim" connote more and increasingly vigorous competition.

And the echoes of political upheavals in every corner of the globe are certain to continue reverberating through it well into the next century.

The constant in assessing and managing these challenges, of course, is your personal involvement. Input from others is vital; but in the end, your decisions will be made on the basis of what you yourself see and hear and understand.

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JOE SIXPACK'S GRIP ON CORPORATE AMERICA

Workers own far more of their companies than previously thought

Last year was a bad one for employee stock-ownership plans. First, Congress abolished some of the juicy tax breaks that made ESOPs popular. Then, the recession dried up the loans many companies use to fund their plans. The most telling sign came in the fall, when UAL Corp.'s unions couldn't line up the funds necessary to buy the airline through an ESOP.

But don't be misled. Employee ownership of Corporate America is thriving, and it goes far beyond ESOPs. In fact, new research shows that if all worker-owned stock is counted, employees have more than \$150 billion worth—and control an average 12% of the 1,000 largest U.S. companies whose employee shareholdings exceed 4%. These figures, which are three to four times previous estimates, suggest that employee ownership is reaching a critical mass that may soon affect how companies are run—perhaps to the surprise of management. "We really haven't thought about issues like employee representation on the board," says Barbara Yastine, the investor-relations director at Primerica Corp., which is nearly 10% employee-owned. "That's not a bridge we've crossed yet."

HIDDEN STAKES. The best evidence of the surprising size of employee holdings comes from *The New Owners*, a new book by Rutgers University management professors Joseph R. Blasi and Douglas L. Kruse. Drawing on more than 20 sources, from filings at the Securities & Exchange Commission to news clips, they found at least \$100 billion in worker-owned stock at public corporations where employee shareholdings exceed 4%. Of this, only \$53 billion is in ESOPs, which are trusts that hold stock for workers. The rest is in pension and savings plans, and even in retirement medical plans, which

some companies are funding with stock.

The authors estimate that employees hold an additional \$20 billion or so in companies where worker ownership is under 4%. What's more, they say, non-ESOP stock-purchase plans, which don't have to be reported to anyone, probably contain \$35 billion more of employee-owned stock. Much of this is invisible to everyone except management, so the size of collective employee holdings isn't obvious. "The rational investor really can't figure out how much employee ownership there is in a public company," says Blasi.

The growth of employee ownership is being fueled by the advantages companies reap. Employee motivation was the reason Primerica set up a non-ESOP stock-bonus plan in 1989 for 1,500 middle managers. The company uses its shares, bought on the open market, to pay up to 50% of annual bonuses. So far, Primerica, which isn't in Blasi and Kruse's data base, has distributed 8.7 million shares to employees—8% of its total. In May, it authorized a 2

million-share buyback that will leave employees with 10% of the company.

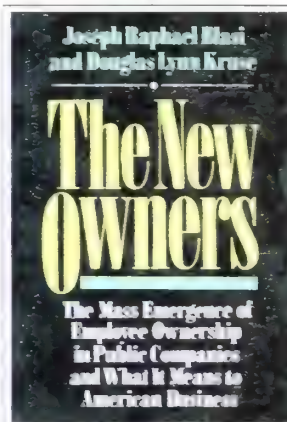
Paying workers with paper can be cheaper than using cash. Sequent Computer Systems Inc. has had several non-ESOP stock plans since it went public in 1983, and today, it is 23% employee-owned. When the computer industry hit hard times this year, the Beaverton (Ore.) company docked its 1,700 employees a week's pay, saving nearly \$2 million. As partial compensation, Sequent gave them stock options that Robert S. Gregg, Sequent's chief financial officer, says will make up for the \$1,000 average wage loss only if the company's stock, now at 15, doubles. "We are not expecting it to double, but it was a way to mitigate the pain," says Gregg.

WIPEOUT. ESOPs continue to spread, too,

partly because they still confer some tax breaks. For instance, companies can still deduct from their taxes dividends paid on stock held in the plan. Morgan Stanley & Co. says about \$10 billion went into ESOPs in 1990. That's down from \$18 billion the previous year. But 1989 may have been an aberration. Takeovers were in full swing, and many companies were setting up ESOPs ahead of the impending changes in the tax code. Indeed, 1990's investment in ESOPs was 50% higher than 1988's, which was 45% above 1987's.

As employee ownership spreads, its ramifications may, too. There can be a downside for workers, such as those at Carter Hawley Hale Stores Inc. More than half of the department-store chain's 24,000-strong workforce pumped thousands of dollars into a savings plan that was billed as a way to support the company after it fought off two takeover attempts. The plan invested exclusively in Carter Hawley Hale stock, giving employees a 40% stake. But in February, the recession prompted the company to file for bankruptcy. Its stock plunged from \$14 a share in 1989 to less than \$2 today—nearly wiping out employee holdings.

Many employers are



WHERE EMPLOYEES ARE THE BIGGEST OWNERS

PERCENT OF COMPANY STOCK HELD BY EMPLOYEES*

By size of employee holdings

Company	Employee stake
MORGAN STANLEY	57%
STONE & WEBSTER	52
OREGON STEEL MILLS	47
GRUMMAN	43
ROCKWELL INTERNATIONAL	41
CENTURY TELEPHONE	39
TOPPS	37
HERMAN MILLER	35
KROGER	34
MCDONNELL DOUGLAS	33

By size of company

Company	Employee stake
EXXON	9%
AT&T	11
PROCTER & GAMBLE	25
AMOCO	6
CHEVRON	16
BELLSOUTH	7
GENERAL MOTORS	9
GTE	9
ATLANTIC RICHFIELD	9
ABBOTT LABS	7

*Includes holdings in pension funds, savings plans, and ESOPs. Ranked by market value

DATA: THE NEW OWNERS SV



TO GET ANYWHERE IN EUROPE, YOU HAVE TO KNOW HOW TO READ THE SIGNS.

The European bank with the most branches outside its home country
continues to insure its preeminence as a universal bank in 1992.

In the past two years, Credit Lyonnais' major acquisitions include
Chase Banque de Commerce/Belgium, Woodchester/
Great Britain and Ireland, Credito Bergamasco/Italy
and a leading position in
the International Moscow Bank.



CREDIT LYONNAIS



NEW YORK • CHICAGO • LOS ANGELES • HOUSTON • SAN FRANCISCO • ATLANTA • MIAMI • DALLAS • BOSTON

trying to minimize the risk by using convertible stock in employee-ownership plans. Convertible shares are usually less volatile than common stock, and they often have a floor value below which the price can't fall. Morgan Stanley says 56% of the ESOPs set up in 1990 used convertible preferred shares, up from 20% in 1988. "They behave more like a fixed-income instrument, so they're less risky," says Paul J. Mazzilli, who heads Morgan Stanley's ESOP strategy group. "But you're still in trouble if the company goes bankrupt."

Employee ownership cuts two ways for employers, too. Workers could provide a source of the patient capital that management has cried out for in the past decade: Workers tend to focus on job security and may therefore be more willing than other stockholders to forgo large quarterly profit hikes so a company can invest for the long term. But one largely unexamined question is whether, in return, employees will demand more input into management decisions. Increasingly, the courts have said that to count in a merger vote, employee-owned stock must be voted by the employees themselves. Adam D. Chinn, an ESOP specialist at the New York law firm Wachtell, Lipton, Rosen & Katz, estimates that perhaps 75% of employee-owned shares can now be voted by the people who hold them.

PROXY APPEALS. It's starting to become clear that managers can't take this for granted. One example: When Grand Metropolitan PLC took over Pillsbury Co. in late 1988, Pillsbury employees voted half of the 1.9 million company shares in their pension plans for Grand Met. Why? Pillsbury's plan to spin off its Burger King franchises angered employees of that division.

There is no legal reason why employee input should be limited to takeovers. In 1989, after Polaroid Corp. set up an ESOP that transferred 19% of the company to employees, a middle manager was named to its board of directors to represent employees. That could be just the start. "As outsiders become more conscious of how much stock employees control, you may see investors targeting employees in proxy fights," says Corey Rosen, director of the National Center for Employee Ownership. "Employees could be given a critical role in corporate governance."

Indeed, employee ownership shows no signs of slowing. Companies are finding new ways to use stock plans all the time, and existing plans are steadily buying more shares. If the next decade brings increases like the past one did, the old socialist dream of employee ownership will become more of a reality than anyone ever imagined.

By Aaron Bernstein in New York

The Corporation

STRATEGIES

NOW COMES SAM HEYMAN, GLOBAL INDUSTRIALIST

He's expanding GAF's chemical business in Europe and Asia

You would be hard put to find a dealmaker whose instincts were so beautifully in sync with the quick-buck mentality of the 1980s. After grabbing control of a floundering GAF Corp. during a proxy battle in 1984, Samuel J. Heyman used Drexel's junk-bond network to launch takeover runs against rival chemical companies such as Union Carbide and Borg-Warner. He never bagged his prey, but he pulled down about \$500 million in profits from his investments. The crescendo came in 1989: Heyman took GAF private in a leveraged buyout valued at \$1.452 billion.

Well, after two years in the quiet groves of private ownership, GAF and its chairman are now bursting back into public view. In late June, Heyman sold 17.8% of GAF's \$512 million specialty chemical unit to the public in an equity offering that raised about \$250 million. But that doesn't mean he's going back into dealmaking. These days, Heyman, 52, prefers to be thought of as an indus-

trialist. In fact, he has grand designs to expand GAF's presence in Europe and the Far East—a move that will put the company into more direct competition with German giant BASF, one of the world's largest chemical companies.

BIG STAKE. GAF's remaining nonchemical operations—a roofing-products business and a New York classical-music radio station—will remain in private hands, namely Heyman's. He invested \$42.5 million of his own money in the GAF buyout back in 1989, and owns 85% of GAF's nonpublic units and 70% of the chemical company. At the market value established by the equity offering, Heyman's stake is

worth more than \$1 billion on paper. So is the public offering merely a golden opportunity for Heyman to cash out? Not a chance, he says. "I've not taken a nickel out since the LBO, and I have no intention of doing so for the foreseeable future," vows Heyman, a former real estate developer and Yale-trained lawyer who worked under Attorney General Robert F. Kennedy.

In fact, Heyman plans to focus on paying down GAF's debt and expanding its promising chemical unit, which now trades under the fancy moniker of International Specialty Products Inc. The stock hasn't budged much from its opening offer of 15½. But investors may be missing something: By all accounts, ISP is a jewel of a niche business.

ISP turns out more than 200 chemical products, mostly additives and enhancers with gobbledygooky names such as gantrez, plasdone, and polyclar. These additives play a variety of roles—from waterproofing to solidifying to

clarifying—and are used in everything from Colgate's anti-tartar toothpaste to Heineken beer. Others strengthen industrial materials such as plastics. "It is one of the best specialty chemical product lines in the world," says Fred Siemer, an independent analyst who tracks the chemical industry.

And as the ISP name suggests, Heyman has big plans to expand GAF's chemical business overseas. He will spend \$75 million to build a plant in Western Europe in 1993. Another is planned in the Far East for sometime in 1995. But with debt at a scary 50% of total capital, ISP will have to move cautiously. What's more, ISP's international fling

A RAIDER'S RESUME

1984 Wins control of GAF in proxy fight

1985 Launches unsuccessful takeover bid for Union Carbide. Profit: \$250 million

1987 Goes after Borg-Warner but comes up short. Profit: \$206 million

1987 Buys and sells 9.8% position in CBI Industries. Profit: \$7 million

1988 Buys and sells 6.2% position in Cabot. Profit: \$23 million

1989 Takes GAF private in a leveraged buyout valued at \$1.42 billion

1991 Takes part of GAF public for \$250 million

DATA. RW

ld yet go awry, as it
es a number of larg-
and more experi-
rivals in Europe.
The biggest threat
them all will come
m BASF, which also
duces a number of
products that ISP
is. BASF is 40 times
size of ISP and is
leading producer of
anediol and tetrahy-
furan—two addi-
tives that contribute
out 5% of ISP's prof-

And BASF is also ex-
tending into higher-
margin products such
as chemical additives
for hair spray. That
has been a long-cher-
ished market for ISP—
and one where the
company has tradition-
ally made a consider-
able amount of money.
GAF has typically any-
where from a 40% to a
50% share in these
markets," declares An-
thony K. S. Raman, an
independent analyst.

AMBITION. Back at home,
GAF Chemical Co., At-
lantic Richfield's petro-
chemical spin-off, is
now moving into ISP's
territory. It has just opened

a new plant in Channelview, Tex., that
will produce the same plastic chemical
additives that ISP puts out.

Even so, there's reason to think that
Heyman's overseas gambit might just
pay off. For one thing, the debt pressure
on GAF's chemical unit is starting to sub-
side. All of the proceeds from the \$250
million public offering will go to pay
down debt. And Heyman says he would
like to pay off an additional \$150 million
of the unit's remaining \$400 million in
debt by 1993. He'll probably have the
cash to do it, thanks to the chemical
unit's current earnings roll. Last year,
operating income reached \$133.1 million,
up 15% over the year before, on sales of
\$1.17 billion. And operating margins,
which have traditionally hovered around
20%, hit 28% during the company's re-
cent quarter.

The recession has pummeled other
specialty chemical makers, but ISP has
survived. It enjoys a dominant position in
a variety of niches. And as the market
cools under among smaller companies, ISP has
gained flexibility. One example is gan-
guly, which is used in Colgate's antitar-
tar toothpaste. ISP is the only domestic
supplier, and the company will raise



HEYMAN: "I'VE NOT TAKEN A NICKEL
OUT SINCE THE LBO"

prices by up to 6% this
year.

Still, ISP sees most of
its future growth com-
ing from beyond these
shores. And to Hey-
man's credit, the com-
pany has already built
up its foreign business.
ISP's overseas sales
have swelled to 50% of
total revenues, from
30%, during the seven
years he has been at
the helm. But aside
from a joint venture
with Hüls of Germany,
most of the company's
foreign sales come
from exports. That
means the company
spends millions on
transportation costs.
So Heyman plans to in-
vest in production fac-
ilities in Europe to get
closer to the company's
customer base and im-
prove profit margins.

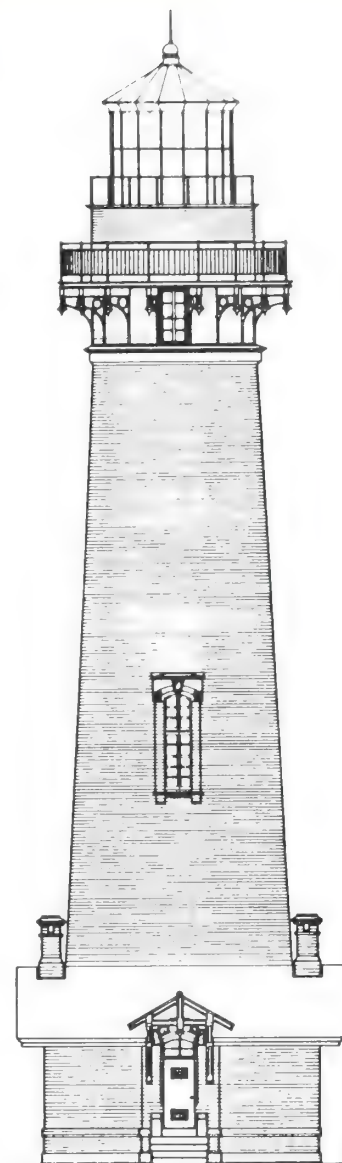
Get Heyman talking
about the Far East,
though, and you'll real-
ly see a gleam in his
eye. He recently
opened sales and mar-
keting offices in China,
Taiwan, Singapore, and
Korea. Heyman pre-
dicts that these fast-
growing Asian mar-

kets will be ISP's most profitable foreign
chemical operations by the end of the
decade.

SMALL WONDER. If Heyman succeeds in
expanding ISP's foreign business, he just
might erase his image as an opportunist-
ic dealmaker. Other factors are helping:
The U.S. attorney's three-year-old insid-
er-trading case against GAF and Vice-
Chairman James T. Sherwin may have
finally run its course. After two mistri-
als and a conviction that was overturned
on appeal, the government has yet to
prove that Sherwin or the company ille-
gally benefited from stock trades made
during the takeover attempt on Union
Carbide Corp. "That whole thing was
an outrage," says one GAF insider. Still,
the government may seek yet another
trial.

After all the excitement GAF experi-
enced during the last decade, small won-
der Heyman prefers to mind his own
business. It may lack the glitz and big
windfalls of raiding. But if ISP's foreign
gambit pays off, Heyman may find that
building his own business is far more
satisfying than trying to snatch someone
else's away.

By Bruce Hager in Wayne, N.J.



PIGEON POINT LIGHTHOUSE SAN MATEO COUNTY CA

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MCI Communications Corporation is the long-distance telephone company that changed the world. It did it by coming up, back in the early 1970's, with a big idea. The idea was to offer long distance service that was less expensive, yet more flexible, responsive and efficient than anything that had ever been offered before.

FACED ENORMOUS CHALLENGES

The company faced enormous challenges and obstacles to realizing its dream, but with great determination it succeeded. And in succeeding it changed the perception of millions of people regarding what a telecommunications company could do. It also opened up the telecommunications industry to a whole new wave of vibrant competition. And then, as country after country saw the electrifying, energizing consequences of deregulating their telecommunications industries, it expanded throughout the world. Today MCI is a giant, with a \$7 billion network—one of the most sophisticated in the world—and operations in 50 countries. And it is growing very fast.

PARTNER IN SUCCESS

MCI's partner in success, almost from the start, has been a company that has

broken through barrier after barrier in telecommunications technology, ultimately developing for MCI, and other customers, some of the most advanced lightwave fiber technology on earth—technology that has enabled MCI to leapfrog all its competitors. The name of the company is Fujitsu. It's a global powerhouse in computers and communications, a visionary force that, with 115,000 employees and operations on every continent, is leading the charge in the worldwide computer and communications revolution—changing the world wherever it goes. And helping its customers change the world, too.



Mr. Richard T. Liebhaber (right), Executive Vice President and Group Executive of MCI Communications Corporation and Paul Tobey of Fujitsu at Fujitsu's head office in Tokyo. Mr. Liebhaber says that Fujitsu's remarkable technological progress has been instrumental in MCI's success. For information call Fujitsu America, Inc. Transmission Division at 1-800-777-FAST

FUJITSU

The global computer & communications company.



RODDICK WITH WODAABE TRIBE MEMBERS IN NIGER: SHE BACKED A DOCUMENTARY FILM ON THE AFRICAN PEOPLE

WHALES, HUMAN RIGHTS, RAIN FORESTS —AND THE HEADY SMELL OF PROFITS

Anita Roddick's 620 Body Shops push causes along with cosmetics

It's a sweltering Sunday afternoon, but the group packed into a conference room at Georgetown University to mark Amnesty International's 30th anniversary numbers nearly a thousand. Clad mostly in rumpled cottons, the youthful crowd has concluded a hand-holding round of *We Shall Overcome* and applauds as a guest speaker moves to the podium. Her name is Anita Roddick, and with a colorful kerchief gathering her mane of dark, curly hair, she seems cut from the same cloth as the people gathered below.

At 48, Roddick may have 20 years on her average listener, but her delivery is as fiery as any young radical's. The Persian Gulf war was a disaster, the fault of "governments that have no backbone." The International Monetary Fund is staffed by tired bureaucrats. Tossing

off aphorisms from Mahatma Gandhi and Ralph Waldo Emerson, she rails at institutions of all stripes. But the Englishwoman saves her sharpest barbs for the cosmetics business. "We loathe the cosmetic industry with a passion," she tells the audience. "It's run by men who create needs that don't exist."

Funny thing, though: Roddick has made herself one of the richest women in Britain by peddling products for those supposedly nonexistent needs. In the process, she has rewritten the rules for the \$16 billion global cosmetics business. Starting with one store 15 years ago, the former schoolteacher has built an empire of 620 shops worldwide, employing a magic formula with two ingredients: Rather than ply her wares at department stores and drugstores—the traditional venues—Roddick sells through

her chain of Body Shops. And instead of appealing to vanity to peddle her potions, she plays on concern for the environment and social issues, offering recyclable bottles and items such as soaps in the shape of endangered animals.

IMITATORS. As managing director of Body Shop International, Roddick is responsible mainly for marketing and product development. But she says her pitch is rooted in a belief that businesses also improve the world. Buy a gourd container for \$6, and you'll help out the indigent Georgia farmer who harvested it. Body Shops stock literature for groups that help save the whales or the rain forest. The cynical view, of course, is that this approach generates prodigious publicity, saving Roddick from having to spend money on advertising—which she claims not to believe in.

either way, her formula is exuding scent of profits. Retail sales for franchised and company stores last year were \$391 million, and earnings, based on wholesale revenues of \$197 million, were \$11 million. Now, rivals are trying to out Roddick at her own game. Powerhouse Estée Lauder Inc. weighed in last year with Origins, a product line that uses "natural" ingredients and recycled containers. Origins opens its first standalone store in July, in Cambridge's Harvard Square. In the past year, The Limited Inc. founder Leslie Wexner opened Bath & Body Works shops that look astonishingly like Body Shop.

Imitation may be a form of flattery, but it must be galling when Roddick is gearing up to open 25 more stores in the U.S. Body Shop now has 100 stores here, but so far they haven't turned a profit because of heavy startup costs. Consultant Allan Mottus says Roddick ought to be consoled: "You don't get too much more competitive than Leslie Wexner and Leonard Lauder."

HEADS. Roddick counters that Body Shop's political agenda will set it apart. And lawyers are in talks with The Limited about the look-alike stores. "People think we're a flaky New Age company," she says. "But my God, we deified ourselves like lions." She also laughs with glee. On Lauder's Origins: "Their environmental concern is nonexistent—give me a break!"

With rivals homing in, another manager might hunker down in the executive suite to plot strategy. But Roddick keeps her frenetic pace, leaving administration to her husband and CEO, Gordon, at the company's headquarters in Littleton, England. A few months' time might see her sniffing out ingredients in the rain forest with Brazilian Indians, filming for a documentary with the Wobe tribe in Niger, and lecturing on whatever cause has her enthusiasm.

Consider two days early this summer: In Washington for the Amnesty International convention, the weekend turns into a typical Roddick whirlwind. First on Saturday is a stop at a store in Georgetown. At 11 a.m., the store is packed, but Helen and Mary Ann Mills, two sisters who bought the franchise a year ago, chat amiably. "Touch my arm," says Mary Ann, glowing from a [unclear] concert. "That's where [unclear] Bob Weir touched me last night." Everyone touches. You get a lot of mileage in a Body Shop out of going to a concert by the tree-hugging Dead.

With their dark green walls and wooden shelves laden with such products as Pineapple Facial Wash, the stores are havens for the environmentally correct. "We call ourselves the grateful dead," adds Helen. "We're grateful to Anita, but we're dead from working so much."

Roddick claims to hate discussing finances—it's "bloody boring," she says—but sneaks in a quiet "How are your sales?" to the store manager. In the next breath: "How is your Amnesty?" (Salespeople help enlist customers for the cause.) The clerk responds enthusiastically. After all, Body Shop's hiring pro-

contributors—into keeping up three orphanages in Romania.

Sunday morning, Roddick is up early for brunch with fellow activist Ralph Nader. The two swap opinions on Presidential politics, and the self-described "Nader groupie" doles out sympathy because "the poor darling" is suffering from a strained back.

That afternoon is the big event. Boosting Amnesty's membership roster is at the top of the Body Shop agenda this semester, so the global activist group has invited Roddick to address its members. The front row is lined with Body Shop employees. Dressed in shorts and Amnesty T-shirts, they cheer lustily as Amnesty leaders address the audience. A closing speaker asks the crowd: "What do you want?" And Roddick onstage bellows with the rest: "Human rights!"

Roddick has always loved a stage. As a child, she worked in her mother's pub in Littlehampton, and her delight in working the crowd led her to dream of becoming "some kind of performer." After college, Roddick tried several careers including teaching and working for the U.N. After marriage, she and Gordon ran an inn and then a restaurant. But when Gordon took off on horseback across South

America in 1976, Roddick chose to support herself and their two children by opening a shop to sell her hand-mixed potions. Did she mind Gordon's trip? Not at all. "I love the grand gesture," she says. "This was not a boring man."

GREEN MACHINE. When Gordon returned a year later, she was preparing to open a third shop. Pragmatism, not activism, dictated how she ran her business. Recycling? "We only had 600 bottles, and we wanted people to return them." Decor? "Green is such a powerful political color—but in the first shop, walls were green because it was the only color that covered the damp patches on the wall."

She's not about to change the formula. Ditto for her style. However much money she makes, however tough the competitive battle, she promises to remain the banner-waver of old. Never shall she waver...well, almost never. Driving to Tysons Corner, the temperature was 95F. "What about the ozone?" she protested as Helen Mills turned on the air conditioning. "Shouldn't we try to do without it?" Dutifully, Mills switched it off. But after 10 blistering minutes, Roddick was wilting—and her principles followed suit. "To hell with it," she said, laughing. "Turn the air conditioning on."

By Laura Zinn in Washington



RODDICK, IN LONDON, CLAIMS TO FIND FINANCES "BLOODY BORING"

cess—during which applicants are asked about everything from personal heroes to literary tastes—ensures employees will be loyal to Roddick's pet passions. She was once about to hire a new retail director, but when she learned he liked to hunt, she sent him packing.

After a lunch of tomatoes and mozzarella at the Four Seasons Hotel, Roddick piles into Helen's car to visit another franchise the sisters own in Tysons Corner, Va. Near the store's entrance is a box of postcards addressed to the President of the Republic of Malawi, appealing for the release of political prisoners. Six months from now, the handouts will be different. Roddick plugs as many hot causes as she can—although she likes only causes that are "easy to understand," choosing a new one every semester. Body Shop currently pumps roughly \$5,000 a month—partly from outside

Boosting Amnesty International's membership is at the top of the Body Shop agenda this semester

SUPER BANKER

NCNB'S HUGH McCOLL IS OUT TO MAKE HISTORY WITH HIS BID FOR C&S/SOVTRAN

Bennett A. Brown couldn't have made himself any clearer. Two years ago, the chairman of Citizens & Southern Corp. rejected a hostile takeover bid for his Atlanta bank from NCNB Corp., telling NCNB Chairman Hugh L. McColl Jr. to "go the hell back to North Carolina." Even though McColl told Brown that he had "launched his missiles," the brash, acquisitive McColl backed off with uncharacteristic meekness. Then, Brown led C&S into a merger with Virginia's Sovran Financial Corp.

How the tables have turned. Stung by unexpectedly heavy loan losses at Sovran and a resulting drop in C&S/Sovran Corp.'s stock price, a chastened Brown was waiting alone at the airport when McColl swooped into Atlanta on June 20 in one of NCNB's corporate jets. The two drove to Brown's home, where McColl did most of the talking. He outlined his plan to merge their companies in a stock-swap deal that would create a bank with more than \$116 billion in assets—exceeded in size among U.S. banks only by Citicorp (table, page 119). McColl, of course, would be CEO. He would call it NationsBank.

NCNB's \$3.8 billion opening bid for C&S/Sovran marks a turning point in banking history. "It radically redefines critical mass in terms of size," says consultant Robert B. Hedges of MAC Group. With vast economies of scale and regional market domination, "these deals will be so compelling that investors will want more of them." Hedges and others argue that the so-called super-regionals can compete directly with the large money-center banks, without the baggage of billions in bad overseas loans and a dependence on loans in maturing urban markets. To many, the combined C&S/Sovran and NCNB operations would be especially appealing because of their solid middle-market lending businesses and their awesome strength in retail banking.

With Congress likely to approve true nationwide banking this year, it's increasingly clear that the key players in the coming consolidation will be super-regionals in towns like Charlotte, N. C., and Columbus,

THE MAKING OF A MAVERICK

1959

Hugh McColl, fresh from the University of North Carolina and the U.S. Marines, joins predecessor of North Carolina National Bank as a trainee

1973

After working his way through various posts, including a prodigious stint as a loan officer in the early 1960s, the aggressive executive becomes vice-chairman of the bank and a director. He is named president of the bank the next year

1983

McColl, who became president of the parent company the year before, takes over as chairman and chief executive. He kicks off a brash acquisition campaign that will spread NCNB throughout the South—and cement his reputation as a dealmaker



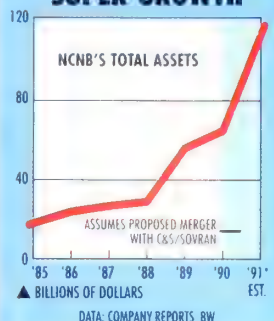
io. Already, super-regionals such as One and First Union have been running up huge market share gains by sticking to the business basics while gobbling competitors. The trend makes sense. The real core banking business is lending locally to consumers and commercial customers," says John B. McCoy, chairman of One Corp. in Columbus.

RISKS. These "nationally active regional banks" are the wave of the future, predicts John S. Reed, chairman of Citicorp. He sees "four or five" money centers, including Citi, Bankers Trust, and Morgan, plus a few big securities firms, staying globally active and focusing on the largest companies. But even Reed

recognizes that money-center banks will face stiffer competition from super-regionals in consumer lending and that the money centers have scant hope of catching the super-regionals in lucrative middle-market corporate lending.

Still, there are huge risks in McColl's plan to form NationsBank. There's the obvious problem of C&S/Sovran's condition. Bad loans now account for 3.3% of its total, up from a far more modest 1.15% at the beginning of last year. And earnings at

A SUPER-REGIONAL'S SUPER GROWTH



McColl's bank also slumped badly in 1990 and would have been nearly nonexistent without the tax-sheltered profits from its Texas operations (page 120). That raises some questions about McColl's ability to manage as assets soar past the \$100 billion mark, especially since he is itching to slug it out with nonbank financial institutions on their own turf. It's a daunting challenge for a team that appears to be stretched thin already.

Yet if there's any banker willing to take a big gamble, it is McColl. Intense, seemingly fearless, and given to outrageous pronouncements, the fourth-generation banker is the closest thing his industry has to Ted Turner. "He's intimidating," says an Atlanta banking consultant who has worked for NCNB. "McColl likes to say, 'We don't meet, we have battles.'"

For years, the ebullient South Carolinian has encouraged the notion that NCNB was destined to be the next Citibank. When some began referring to NCNB as the Citibank of the South, McColl twisted it around and began calling Citibank "NCNB of the North."

He specializes in takeovers: In his eight years as CEO, McColl has strung together more than 100 deals. His most dramatic, the 1988 takeover of Dallas' First RepublicBank Corp., more than doubled the size of Charlotte-based NCNB. Today, Texas accounts for much of its earnings.

McColl, 56, is purposely maintaining a low profile

these days, hoping to avoid unleashing the kind of inflammatory comments that have antagonized adversaries and scuttled earlier takeover attempts in Georgia, Tennessee, and Florida. He once criticized Florida bankers for being lazy, and on another occasion, he told Georgians that he wasn't going to follow "every pig path" in the state to create a big bank there. McColl declined to be interviewed for this story. But his vision is clear—and it extends well beyond C&S/Sovran.

McColl is the most vocal proponent of a radical plan now being endorsed by a few other maverick bankers. He's pushing for NCNB to be allowed to operate a separate, freewheeling merchant bank that would not be protected by the Federal Deposit Insurance Corp.'s safety net. In exchange, NCNB would be permitted to compete head-on with investment banks such as Morgan Stanley and Salomon Brothers, insurers, and corporate-owned financial institutions such as GE Capital Corp. McColl sees this unit underwriting securities, selling insurance and mutual funds, and being a larger player in takeovers—all with funds raised from private capital markets.

MASTERSTROKE. McColl will have to cool his heels before implementing this vision, however. The core bank/merchant bank concept is not part of the bank-law overhaul legislation approved by the House Banking Committee on June 28 and is unlikely to pass this year. But if the bill does make it to President Bush's desk with the provision allowing for true interstate banking and interstate branches, there will be more than enough activity to keep McColl and his troops occupied. A regional compact already allows NCNB to acquire other banks in several Southeastern states, plus failing institutions nationwide. But now, a merger SWAT team reporting to NCNB Chief Financial Officer James H. Hance Jr. is studying several potential takeovers, including Southeast Banking Corp. of Miami.

For now, McColl's initial C&S/Sovran merger proposal calls for exchanging each of C&S/Sovran's nearly 137 million shares for 0.75 of an NCNB share, or about \$27.75 a share based on NCNB's current stock price. Both banks have more than \$1 billion in nonperforming loans on their books, so the final exchange offer might depend on how effectively each side can convince the

1985

NCNB tries to buy First National Bank of Atlanta, but its directors accept a slightly lower offer from Wachovia Corp.

1988

Sensing a bargain, McColl snares deeply troubled First RepublicBank Corp. of Texas, with \$32.5 billion in assets. Huge tax benefits shelter future earnings, and the FDIC scoops up billions in bad loans

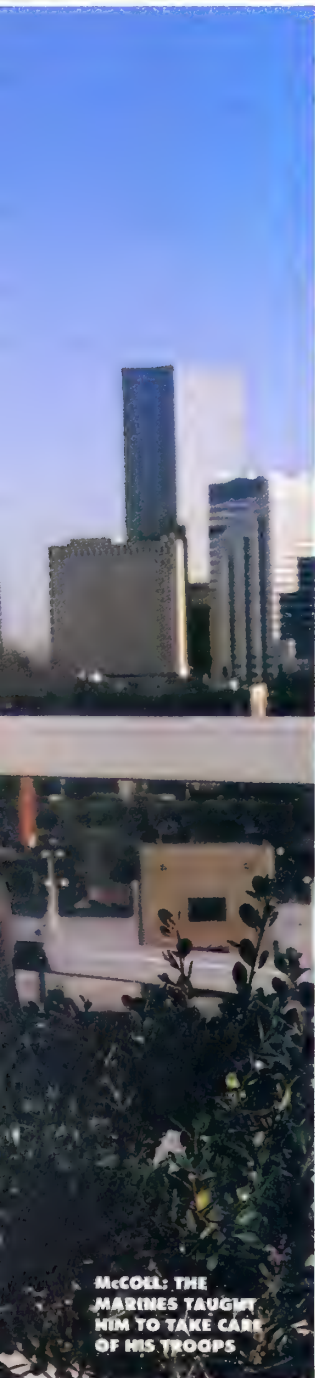
1989

McColl tries to buy genteel Citizens & Southern, Georgia's largest bank. It shoos him away and merges with Virginia-based Sovran Financial at a price lower than NCNB's offer

1991

He's back. When C&S/Sovran stumbles on some bad loans, McColl re-surfaces ready to talk merger again. C&S Chairman Bennett Brown, no great fan of McColl's, agrees to merger discussions

DATA: BW



McCOLL: THE MARINES TAUGHT HIM TO TAKE CARE OF HIS TROOPS

other of the strength of its balance sheet. Also, NCNB can't exchange much more stock than McColl proposes or it could lose valuable tax benefits.

In strategic terms, the acquisition of C&S/Sovran, with its network of nearly 1,000 branches concentrated primarily in Georgia and Virginia, would be a masterstroke for McColl. Paired with NCNB's Southeast strongholds in North Carolina and Florida, C&S/Sovran would give NCNB dominance from Baltimore to Key West, Fla., complementing its No. 1 position in Texas and giving it an industry-leading total of more than 1,900 branches. The middle-market lending strengths of both banks would get a boost from NCNB's savvy in back-office productivity and C&S/Sovran's expertise in specialized receivables lending.

DAUNTING TASK. There would be lots of room for cost savings as well. Bear Stearns & Co. analyst Mark Alpert estimates that NCNB could chop at least \$130 million in yearly overhead by eliminating duplicate branches in South Carolina and Florida and perhaps as much as \$150 million more by consolidating headquarters and back-office operations. Assuming that McColl's troops could pull off the daunting task of integrating the two companies smoothly over the next few years, NCNB would be ideally positioned to march north and west by 1994, when full interstate banking is expected.

But that's a towering "if." The soured pairing of C&S and Sovran illustrates how difficult bank mergers can be. Management has wrung out few if any inefficiencies. Instead, executives have been forced to concentrate on trying to stanch the hemorrhaging from Sovran's problem real estate loans. The culture clash at NationsBank could be just as troublesome. NCNB is a competitive environment where employees are encouraged to take risks. C&S/Sovran is a far more genteel, careful company. Consultant David C. Cates of Ferguson & Co. in Washington worries that McColl may be biting off a bit too much this time. "NCNB has a very special and superior culture," he says. "They are the best and the brightest. The thing is, C&S is the same way. The chemistry challenges are enormous here."

McColl and his managers haven't exactly been subtle when it comes to dealing with culture clashes. NCNB gained a reputation for toughness when it ousted line officers at banks it acquired in Florida in the 1980s and replaced them with hard-charging

young McColl clones. NCNB officials say they've learned from their mistakes, but McColl's rivals aren't about to let him—or anybody else—forget it. NCNB's archcompetitor, Wachovia Corp., based in Winston-Salem, N.C., recently agreed to acquire \$7.1 billion of South Carolina National Corp.'s assets in a stock swap that will boost Wachovia's assets to \$32.7 billion. Discussing the deal, Chairman John G. Medlin Jr. took a pointed swipe at McColl and NCNB: "For now, we'll continue to follow a gradual expansion plan across the Southeast at a pace that allows for quality mergers done in a humane manner."



C&S/Sovran's Brown: Loan losses led to reluctant talks with McColl

NCNB's reputation may yet derail the NationsBank idea. According to one C&S/Sovran director, a sizable contingent on the 29-member board wants to stay independent. "Who knows what the value will be of the paper [NCNB stock] we'll be getting if we say O. K.?" asks the board member. "If we can put our real estate problems behind us, in three years, we'd be in the catbird seat with the market franchises we have." But Brown may take a more bottom-line approach. Brown, who declined to be interviewed for this story, gave a crisp, unemotional presentation at a special June 27 board meeting at which he was given the go-ahead for formal negotiations with NCNB. Brown repeatedly told the board that his recommendation will be based on what is best for the shareholders.

While both sides say they have put no time limit on the due-diligence process, C&S/Sovran's next scheduled board meeting on July 16 looms as a practical deadline. That's when the board is slated to de-

cide whether to slash the quarterly common stock dividend because of continuing loan losses. Second-quarter earnings have not been released yet, but C&S/Sovran has already publicly confirmed that nonperforming assets—loans not expected to be paid back in full—will rise in the period, albeit by less than the first quarter's \$403 million increase. If the worsening loan situation forces the board to cut its dividend and C&S/Sovran's stock price plunges sharply, McColl's lifeline may be the only practical alternative.

For McColl, that victory would be especially sweet. He and Brown are natural rivals—both are South Carolinians and have known each other for almost three decades. McColl was born six years after Brown and 60 miles north, in Bennettsville, S. C. His great-grandfather organized a bank there after the Civil War and built a railroad with the lofty name South Carolina & Pacific. It ran all of about 50 miles.

McColl's father eventually liquidated the bank and concentrated on cotton farming, but banking remains in the family's blood: Both of McColl's brothers are bankers. (One works for C&S/Sovran in Columbia, S. C.) Both of McColl's sons are in the business, too. His oldest, Hugh III, is an investment banker at Bear Stearns in New York. Hugh III was pitted directly against his father during the 1988 battle for control of First Republic. Dad won.

POKER MARATHONS. At the University of North Carolina in the 1950s, McColl was an indifferent business major. C. R. May III, a fellow member of Beta Theta Pi fraternity, recalls that McColl was noted for presiding over round-the-clock, penny-ante poker marathons that he usually won. "Money was never the motivation," says May. "Making you quit first was."

After graduating in 1957, McColl volunteered for a two-year stint in the Marines. He has often said it forever changed his life. Talking to a reporter in 1990, McColl remembered what it was like to live with non-Southerners for the first time. "I hated Yankees growing up," he said. "I was raised [to believe] they burned our fields and houses, raped our women and destroyed our economy, and held us in involuntary servitude for 100 years—some of which is true."

More than anything, though, McColl has said that the Marines taught him to take care of his troops at all cost. That's why NCNB was one of the earliest proponents of

able-benefit programs
t help reduce turnover
ong young mothers in
rical and teller jobs.
d it's also why he
od by Timothy P.
rtman in 1985 when
rtman was forced to
e a leave of absence
ile the Securities &
change Commission in-
gated his role as
ef financial officer in
bankruptcy of Bal-
in-United Corp. Hart-
n was cleared, and
o years later, he helped come up with
tax-saving gambit that helped NCNB
the bidding for First Republic. Today,
s vice-chairman of NCNB.

MILITARY-LIKE. Luckily for McColl, his
ntors at NCNB encouraged him to break
mold. Perhaps sensing that he would
this kind of freedom, McColl politely
urned an offer from his father-in-law to
rk at a small family-owned bank when
got out of the Marines and instead let
father arrange an introduction at what
ame North Carolina National Bank.
chovia Bank & Trust Co. had long had a
nk on corporate lending in North Caroli-
so the upstarts at NCNB did to blaze
ir own trail.

Early on, McColl caught the eye of NCNB
 chairman Addison Reece and his succes-
 Thomas I. Storrs. McColl was named
sident at the age of 39. Once he made it

WHERE McCOLL'S 'NATIONS BANK' WOULD FIT IN

Total assets as of Mar. 31	
	Billions
CITICORP	\$216
NATIONS BANK	116*
BANK OF AMERICA	112
CHASE MANHATTAN	98
J.P. MORGAN	94
SECURITY PACIFIC	83

*Combined assets of NCNB and C&S/
Sovran

DATA: COMPANY REPORTS, BW

to the top nine years lat-
er, McColl wasted little
time in stamping his im-
print. "He doesn't mind
stepping on egos, arms,
or legs to reach his objec-
tive," says a former
NCNB executive.

McColl accelerated a
program of hiring legions
of MBAs, effectively
bringing in nonbankers
to challenge older staff
officers. Gordon W.
Campbell, who was CEO
of Florida-based Ex-

change Bank when NCNB acquired it, calls
McColl's recruits "very military-like.
They'll run through walls if McColl tells
them to. He doesn't have a lot of tolerance
for incompetence."

Once, a colleague recalls, McColl visited
a department at headquarters and noticed
a young employee sitting in a broken chair.
He inquired, and she told him she had put
in an order almost two months earlier.
McColl picked up a nearby phone, dialed a
senior executive in charge of purchasing,
and told him: "If you can't get her a chair
in the next 15 minutes, bring her yours."

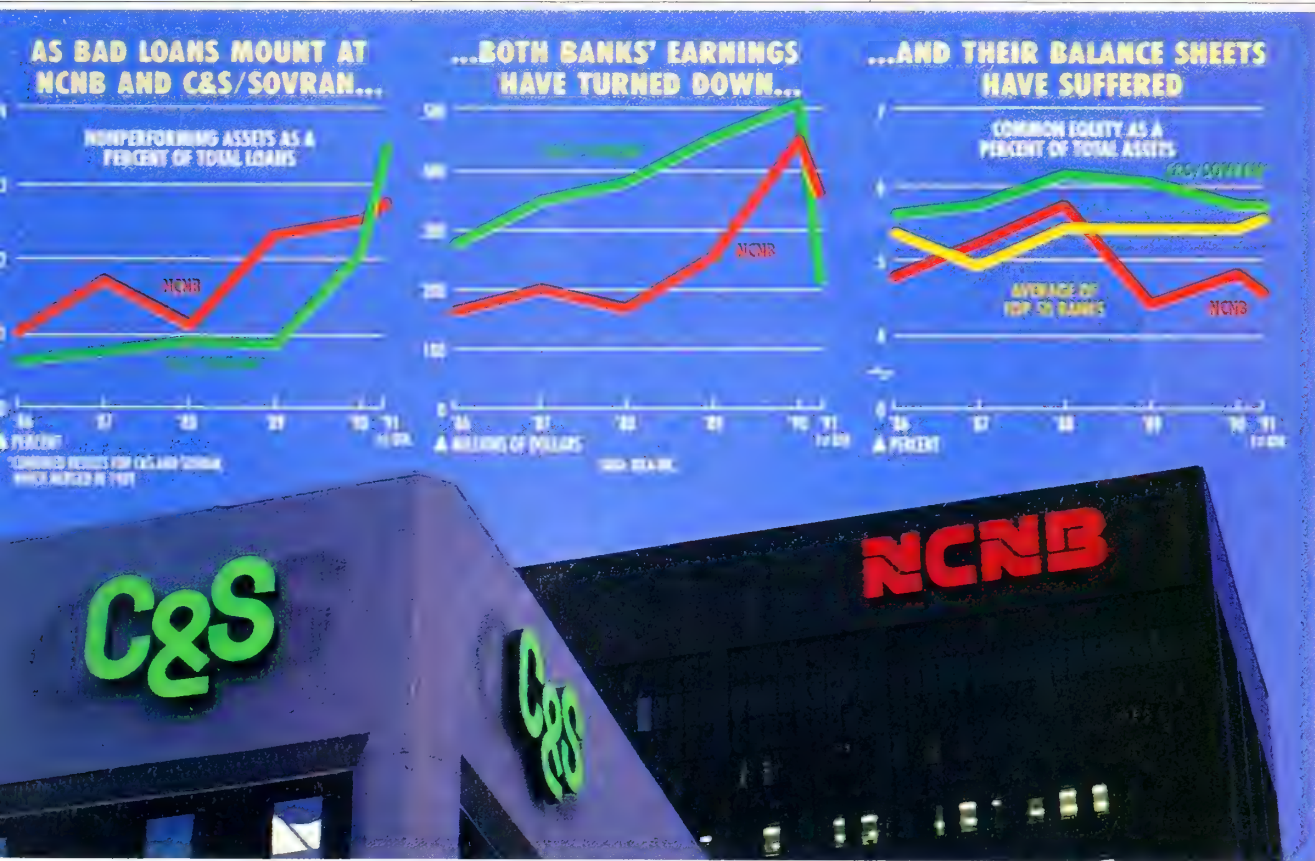
Imagine the reverse image of McColl's
supercharged style, and you have the ap-
proximate measure of Bennett Brown. A
former bank examiner, Brown took over
Citizens & Southern on an interim basis af-
ter the 1975 recession decimated its portfo-
lio of real estate loans.

Brown's housecleaning saved the bank
and earned him a full-time job as CEO. But
former executives criticize Brown for fail-
ing to reenergize the bank in the 1980s, vir-
tually guaranteeing that it would be a
takeover target. Worse, in running away
from McColl and into a hasty marriage
with Sovran two years ago, Brown and C&S
ended up getting blindsided by a real es-
tate loan mess that was brewing at Sov-
ran's three banks in the Washington area.

NO BRAKES. Analysts at Atlanta brokerage
Robinson-Humphrey Co. pin the blame on a
lack of strong centralized credit controls at
Sovran, itself the product of a 1984 merger
of banks in Norfolk and Richmond. As a re-
sult, when Sovran's Washington-area
banks went on a commercial real estate
lending binge starting in 1987—about the
time that even Texas savings and loans
were exiting that overheated market—no-
body put on the brakes.

McColl ought to be somewhat sympa-
thetic to Sovran's plight. For years, NCNB
has been willing to make loans to custom-
ers that other banks viewed as too risky. It
almost ensured that a higher percentage of
loans would go sour, but at the higher
rates the bank was charging, the net effect
was worth it—especially since NCNB was
an industry leader in back-office productiv-
ity improvements. The formula came un-
hinged last year, though, when losses on
real estate loans began to mount.

Once the staggering size of the problem
became clear—\$1.03 billion in nonperform-
ing loans—McColl moved quickly. He bor-



HOW NCNB SWEEPED THROUGH TEXAS —WITH A LITTLE HELP FROM THE FEDS

When NCNB first moved into Texas in 1988, the North Carolina outsider didn't exactly get a hero's welcome. Instead, it got jeers from the local populace, hostility from the state's independent bankers, and criticism in Congress for its sweet deal to acquire the remnants of failed First RepublicBank Corp.

Yet NCNB Corp.'s bold bid for the state's largest banking company has clearly paid off. Last year, NCNB made virtually all of its \$366 million in profits in Texas. This year, NCNB Texas National Bank could generate at least half of its parent's earnings, estimates bank analyst Anthony J. Polini of A.G. Edwards & Sons Inc. Indeed, earnings at the Texas unit have allowed NCNB to be aggressive about charging off problem loans in the Southeast. "Products and service matter a lot more than where you're from," says Kenneth D. Lewis, president of NCNB's General Bank, which oversees seven state banks.

Much of NCNB's success in Texas stems from the savvy deal the bank negotiated with federal regulators. The Federal Deposit Insurance Corp. kept First Republic's bad assets, and NCNB won guarantees that limited its losses on the loans it kept. A controversial ruling from the Internal Revenue Service handed NCNB \$2.8 billion in tax benefits. "The way it was structured, there was no way you could lose money," says analyst Frank W. Anderson of Stephens Inc.

STILL PROWLING. NCNB hasn't stopped with First Republic. Since swallowing that bank's 40 units, it has snatched up 19 savings institutions with more than \$7 billion in deposits. NCNB's network has swollen to nearly 300 branches across the state—a big advantage in luring consumers. With \$33 billion in assets, NCNB Texas is nearly twice the

size of its closest rival and is still prowling for more failed thrifts.

NCNB has also moved aggressively to market its expertise in collecting on problem loans and foreclosed properties. As part of the deal for First Republic, NCNB set up a collections unit to handle the job for the FDIC. The agency covers the losses and pays direct expenses, plus incentives based on the amount collected. In the past two years, NCNB has pulled in \$72 million



NCNB's Dallas headquarters

in management fees for its \$4.2 billion in cash collections. With the original pool of bad assets dwindling, NCNB is hunting for new customers. It has contracts to manage more than \$2 billion in assets for Resolution Trust Corp., which oversees the S&L bailout.

That could benefit NCNB if it wins its bid for C&S/Sovran Corp. But NCNB's collection effort has cost it plenty of goodwill in the Lone Star State. One Abilene man spent nearly a year picketing NCNB branches after his business loan

wound up in the collections pool.

NCNB's image problems don't end there. Community bankers charge that its tight lending practices are holding back Texas' fledgling recovery. The Independent Bankers Assn. recently asked the Federal Reserve Board and the comptroller of the currency to investigate NCNB's lending in the state.

Meanwhile, rivals complain that its hefty tax breaks allow NCNB to pay more for deposits, charge less for loans, and bid higher for acquisitions. "The subsidy makes it tough for us to compete," says Gary G. Jacobs, CEO of Laredo National Bank, with \$1.1 billion in assets. The good news for the little guys: NCNB's tax benefits may run out in the next two years. The bad news: Even without the tax benefits, NCNB is among the fiercest competitors around.

By William Z. Foster in Dallas

rowed a page from the Texas playbook and set up an asset-disposition bank in the Southeast headed by William P. Middlemas, the president of Southeast banking. He was told to get rid of the problem fast—and not to worry unduly about offending longtime customers.

Owning up to the mess hit McColl directly in the pocketbook. Higher loan-loss provisions contributed to an 18.2% plunge in 1990 net income, to \$365.7 million. So McColl and most other top NCNB executives didn't get a bonus for the year. (In 1989, McColl's bonus was \$875,000.) There was a small consolation, however: His base salary rose from \$625,000 in 1989 to \$700,000 last year.

HUMBLED. Particularly embarrassing is the fact that most of the problem real estate loans are in Florida and North Carolina, where NCNB lenders presumably know the local markets best. Humbled ever so slightly, McColl now says his goal is to generate half of NCNB's future loan demand in what he calls the "core bank"—from the relatively mundane businesses of home mortgages, credit cards, car loans, and other consumer offerings.

Out of the office, McColl is equally intense. Whether it's drinking beer with trainees, playing on the company softball team, or serving on the board of small Queens College in Charlotte, colleagues say he's always "on." His friend V. Rietzel Snider, a Charlotte real estate investor, has played racquetball with him and lived to tell the tale. "Hugh is a white-hot blowtorch as a competitor," says Snider. "He plays with absolute abandonment, crashes into a wall, bleeds awhile, then gets up."

As for the future, McColl hasn't let on how long he'll stay on as chairman. If he imitates his predecessor, retirement is at least nine years away. That hasn't stopped NCNB-watchers from trying to handicap the succession race. The death from a brain tumor of onetime heir apparent Francis "Buddy" Kemp in 1990 has turned the spotlight to Kenneth D. Lewis, who was running NCNB Texas and is now back in Charlotte as president of General Bank, overseeing NCNB's seven state banks.

But a lot is sure to happen before McColl walks away. It's possible that an executive from C&S Sovran could even percolate to the top if the deal goes through. That would assuage only somewhat the wounded pride of C&S veterans in Atlanta, who were looking forward to moving into a new, 55-story headquarters building next year. The thing is, McColl is overseeing construction of a new 60-story headquarters in Charlotte that the locals call the Taj McColl. Like it or not, C&S Sovran may soon have to call it home.

By Chuck Hawkins in Atlanta and Dean Foust in Charlotte, with Zachary Schiller in Cleveland and Peter Finch in New York

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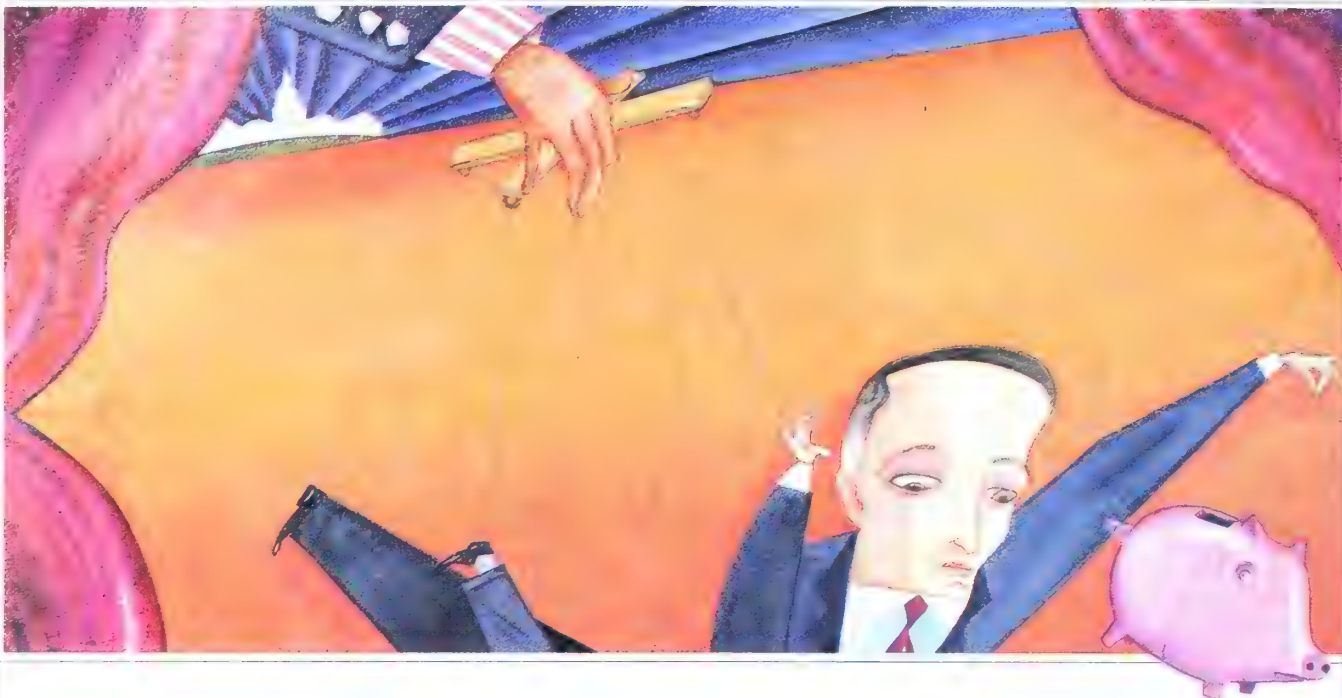
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REFORM, OR A CRACKDOWN ON BANKING?

A bill in Congress would put a choke chain on regulators and impose harsh constraints on ailing banks

The banking reform package wending its way through Congress is widely seen as a virtual wish list for banking. The version approved on June 28 by the House Banking Committee, which has a long way to go before becoming law, would open a lot of doors for banks. It would allow them to branch into other states and enter a passel of new businesses, from securities underwriting to insurance. But buried in the measure are harsh proposals that would have a quite different impact. They would impose stiff constraints on banking regulators and crack down, probably too soon, on banks that fall on hard times.

Stung by the lax supervision that led to the savings and loan debacle, lawmakers have decided that the banking industry's cops can't be trusted to be tough with the banks on their own. The Federal Deposit Insurance Corp.'s request for a \$70 billion loan to bail out the agency's ailing insurance fund has made Congress even more antsy. "Regulators blew it in the '80s," says Representative Charles E. Schumer (D-N. Y.), a member

of the Banking Committee. "They took 50 years' credibility and lost it."

A mechanism in the bill would require regulators to move swiftly when banks start to deteriorate, preventing government dithering that at times lets bad situations get worse. The further a bank falls short of certain requirements for capital, asset quality, and earnings, the more the government overseers have to do: freeze growth, stop dividend payouts, and curb executives' salaries and bonuses. The Treasury Dept., author of the reform plan, thinks regulators could be more hard-nosed. Says a senior Treasury official: "It would be healthy to have a clear road map, which sets out actions for regulators."

GOOD RECORD. But many critics think that the clamping down on regulators goes too far. "Congress cannot micromanage banking in its attempts to respond to the current crisis," says Kenneth A. Guenther, executive vice-president of the Independent Bankers Assn. "Once the crisis is over, it will have put in a set of guidelines that may not work."

The Office of the Comptroller of the Currency argues that regulators have a good track record of letting shaky banks rejuvenate themselves without tapping the bank insurance fund. OCC official Leonora Cross says that if the toughest standards had been in effect when Bank of America got in trouble, "Bank of America would not be here today." Regulators kept the San Francisco bank open during its worst days in the mid-1980s, and now it is one of the most successful in the country. The reform bill does allow some leeway, letting regulators circumvent some mandated actions if they deem it necessary. But they may have to explain themselves before Congress—not an appetizing prospect.

Industry experts complain the legislation undercuts the flexibility of bank executives. It could prompt banks with battered loan portfolios to use their available resources to rebuild capital instead of reserves set up to absorb loan losses. The bill "will end up not only eliminating regulatory discretion but managerial discretion as well," says

Washington banking consultant Karen Law.

The bank bill's strictures make sense at least one area: curbing the Federal Reserve Board's lending to ailing banks at the discount window. The Fed used to prop up such sick banks as Boston's Bank of New England and Washington's Madison National Bank. The House Banking Committee found that the Fed has \$8.3 billion in loans outstanding at 320 banks. Since it has first claim on bank assets, the Fed gets its money back. Many depositors—whose accounts exceeding \$100,000 aren't insured—were happy: The banks used the Fed money to pay them off. Yet that left the FDIC holding the bag. "This is a massive form of forbearance granted in secret by the Federal Reserve," fumes

House Banking Committee Chairman Henry B. Gonzalez (D-Tex.).

Faced with the threat of strict limits on discount-window lending, Fed Chairman Alan Greenspan struck a deal with Gonzalez. Under the bill, if the Fed wants to lend to a bank for more than 60 days, either the Fed chairman or the bank's top regulator must certify that the bank isn't failing. If the bank then goes under, the central bank would have to reimburse the FDIC for any losses caused by discount-window loans. The impact of that compromise could force the Fed to back away from its "too big to fail" stance of propping up the largest banks at all costs.

OVERDUE. The reform bill also is sensibly tough on the disposal of failed banks. It calls for the FDIC to choose the least

expensive method, which would likely mean dissolving the institutions and selling their deposits for a premium to other banks. Under current law, the FDIC typically prefers to keep failed banks intact by selling them to investors, believing that this better serves the community and protects the financial system.

Moves to strengthen bank oversight are overdue. Forcing prompt regulatory action, especially if banks are allowed into new businesses, may well be a sound approach. But regulation, like banking, is a judgment business. If Congress writes rules that are too rigid for the new era of financial services, it may win the war of the '80s—and lose the war of the '90s.

By Catherine Yang and Mike McNamee in Washington

THE FDIC KEEPS DIGGING A DEEPER HOLE

No wonder Congress is suspicious of bank regulators. Every few months, it seems, the regulators add a few billion dollars more to the cost of the bank bailout and the probable hit on the Federal Deposit Insurance Corp.'s bank insurance fund, which runs busted banks and pays off depositors' accounts. Growing evidence that the regulators don't yet have a handle on the problem suggests more unpleasant jolts could be on the way. It seems increasingly likely that the fund may have to be bailed out by taxpayers, who lately are picking up the tab for the savings and loans.

In January, the FDIC said the insurance fund's assets at the end of 1992 could range from \$3.6 billion in the black to \$4.6 billion in the red. That's a big slide from the \$18.3 billion the fund had at the end of 1987. Now, the FDIC says that the balance could range from a \$3 billion deficit, if things are going well, to \$11 billion in the hole (chart), if they aren't. The agency is asking for a \$70 billion federal loan to bail out and resuscitate the fund.

WORST CASE. The fund numbers keep getting worse because the agency's outlook for the banks keeps growing more dismal. In January, under its most pessimistic scenario, the FDIC forecast that 440 institutions, with a total of \$160 billion in assets, would collapse through 1992. On June 27, using updated economic data, FDIC Chairman L. William Seidman shook up lawmakers with an increase of \$40 billion—or 25%—in the

estimated assets involved, to \$200 billion at 400 busted banks. The FDIC responds to carping about its shifting numbers by arguing that all predictions are elusive. Says Roger Watson, the FDIC's research director: "Seidman's an honest guy."

Maybe so. But it's a good bet that the size of the FDIC insurance fund's bailout will balloon still further. The Administration's \$70 billion figure doesn't include interest, which could add an estimated \$40 billion to \$50 billion by 2006. Projected interest costs have inflated the \$160 billion the government has borrowed for the S&L cleanup to \$500 billion over 40 years.

The insurance fund itself may already be in even worse shape than the FDIC has been saying. Congress' General Accounting Office contends that the FDIC still overstates the fund's assets by posting losses too slowly. The fund waits until regulators move to close a bank instead of acting as

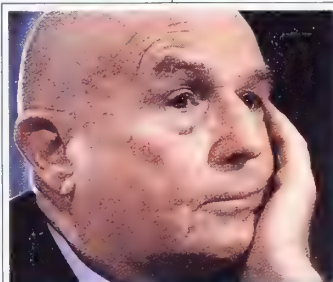
soon as it becomes insolvent. By the quicker method, the fund's 1990 yearend balance would have been a bit more than half of the skimpy \$8.4 billion posted last winter. The FDIC is now tacitly conceding the point: It recently lowered the 1990 balance by \$2 billion.

UNDER WATER. Worse, the banking industry's health may be more precarious than the FDIC admits. Reason: Banks' capital cushions, which they use to offset losses, may be overstated. If banks carried assets at actual market value, rather than at the (currently higher) original cost, far more banks would be under water. Then, says Edward Kane, banking professor at Ohio State University, the insurance fund would show a 1990 deficit of \$40 billion. True, the banks' plight is not nearly so dire as the thrifts'. Banks are better run, regulated, and capitalized. Even so, 1,000 banks have failed in the past five years.

Government officials claim that taxpayers needn't worry: The recovering economy will allow weak banks to grow out of their precarious positions. Healthy banks will eventually rescue the fund through increased deposit-insurance premiums. Regulators have already boosted the rate, effective July 1, to 23¢ per \$100 in deposits, up from 19½¢—a change that will net the fund \$10 billion a year. Perhaps. But some experts warn that this is straining the system and that another premium hike could crimp lending, creating an economic slowdown and more bank failures.

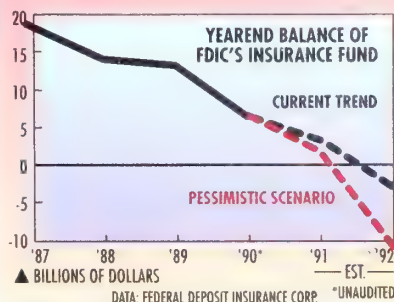
Without convincing evidence to the contrary, the Cockroach Theory of Economics still seems applicable here: Once you've seen one piece of bad news, more will follow.

By Catherine Yang in Washington



SEIDMAN: THE AGENCY IS ASKING FOR A \$70 BILLION LOAN

THE EVAPORATING BANK-RESCUE FUND



THEY LOVE STOCKS THAT ARE ALL BEATEN UP

Take IBM: It's way down, but a big dividend lures 'value' investors

For most of his 26 years on Wall Street, Byron R. Wien has been an IBM booster. After all, IBM was the quintessential growth stock, and isn't growth what investing in equities is all about? But on June 19, Wien, the U.S. portfolio strategist for Morgan Stanley & Co., threw in the towel and told his clients to dump Big Blue. "I want to own companies that are getting stronger, not weaker," says Wien. "I could no longer see why I was holding IBM."

Neither can most of Wall Street. The stock has plunged from nearly 140 in March—it sold as high as 175 in 1987—to 99 now. But as disillusioned growth investors abandon IBM, the stock is finding a home in the portfolios of "value" investors who buy beaten-up stocks. They look for stocks that are cheap relative to such yardsticks as the price-to-earnings ratio, the price-to-book-value ratio, or—perhaps most important in IBM's case—the dividend yield. Value strategists are contrarians, since value stocks become cheap precisely because the crowd shuns them.

Roger Newell and Brian C. Rogers are snapping up IBM. They like the \$4.84-per-share dividend, a juicy 4.9% yield. That's about 50% greater than the dividend yield of the stocks in the Standard & Poor's 500-stock index and nearly 90% greater than that of the average industrial company.

A POUNDING. Neither Newell, whose Newell Associates manages about \$900 million, including the \$480 million Vanguard Equity Income Fund, nor Rogers, who runs the \$1.1 billion T. Rowe Price Equity Income Fund, would settle for 5% if there were no hope the stock would appreciate. And no matter how high the yield, they wouldn't invest in a stock unless the dividend looked secure.

As the stock has been pounded over the past few months, value investors' interest perked up—in retrospect, a bit too soon. "Much to their chagrin, the value managers got interested in IBM when the stock was in the \$110 to \$115 range," says Robert Moseson, president

of Performance Analytics Inc., which keeps tabs on the performance of some 1,500 investment managers. "They see it as a money-market fund with the potential for 10% to 15% a year appreciation."

Shearson Lehman Brothers Inc. also likes IBM. On July 1, the stock won a place on the firm's "Ten Uncommon Values" list. Shearson is taking a contrary view of IBM's mainframe computer business, which accounts for 65% of sales. "Mainframes are not dinosaurs," says Fred Fraenkel, Shearson's research director. He thinks IBM's fortunes will turn up sharply in the fall, when it

1984, and 1986, though only slightly in 1989 and 1990. But so far this year, high-yield stocks are trailing the market by about 3.9 percentage points.

Followers of the dividend-oriented strategy also like the reduced risk. According to Jones, the "beta" is 0.82. That is, when the market goes up, the high-yield portfolio enjoys only 82% of the upside. But when the market tanks, the portfolio takes only 82% of the fall.

Of course, the dividends have to be secure. Wien says with earnings coming down and the near certainty of more layoffs and write-downs, IBM's "dividend may be in jeopardy." T. Rowe Price's Rogers says the least of his worries is IBM's payout. The risk in Big Blue, he says, is that the company may fail to benefit from the economic recovery and the stock continue to languish.

UNENTHUSIASTIC. Given current interest rates, the high payout would probably be attractive to enough buyers to keep the stock from dropping much further. "It's hard to imagine IBM selling at greater than a 5.5% yield," says Susan Wilder, portfolio manager of the \$1.4 billion Oppenheimer Equity Income Fund. To reach a 5.5% yield, about what money-market funds are paying, IBM would have to drop to \$88.

Although she owns IBM, Wilder's position is hedged with options, and she may sell it when the options expire later this month. A better yield stock, says Wilder, is Asarco, a copper producer, which sports a 6% payout. "Asarco has already been restructured," she says. "So it should do better in an economic recovery."

Other stocks favored by yield-oriented portfolio managers are Eastman Kodak, Westinghouse, and Xerox. Westinghouse, as a cyclical company, has long been a high-yielder. But Eastman Kodak and Xerox are a lot like IBM—one-time growth stocks that have lost their ways. While Kodak is down

SOME HIGH-YIELD BLUE CHIPS

Stock	Price	Dividend	Yield
ALLIED-SIGNAL	34 $\frac{5}{8}$	\$1.80	5.2%
ASARCO	26 $\frac{5}{8}$	1.60	6.0
DOW CHEMICAL	54	2.60	4.8
DUN & BRADSTREET	46 $\frac{7}{8}$	2.16	4.6
EASTMAN KODAK	39 $\frac{5}{8}$	2.00	5.1
IBM	99 $\frac{1}{8}$	4.84	4.9
SEARS	38 $\frac{1}{2}$	2.00	5.2
TEXACO	61 $\frac{7}{8}$	3.20	5.2
WESTINGHOUSE ELEC.	28 $\frac{3}{8}$	1.40	4.9
XEROX	54 $\frac{1}{2}$	3.00	5.5

DATA: BRIDGE INFORMATION SYSTEMS INC.

starts shipping new mainframes. He, too, likes IBM's fat dividend. "That's a big difference between IBM and most other technology companies."

History shows that investing in battered high-yield stocks is a very rewarding strategy. Buying big stocks with higher-than-average yields would have beaten the market easily over the last decade, says Robert C. Jones, a quantitative analyst at Goldman, Sachs & Co. From 1981 through the second quarter of 1991, the strategy delivered an average annual return of 19.6%, vs. 15% for the S&P 500. A high-yield portfolio outperformed the averages handily in 1981,

only 4.8% this year, Xerox, which sold with an 8% yield in January, has climbed 53.5%. Dun & Bradstreet is a relatively new name on the high-yield list. "They're having to do some restructuring," says James H. Gipson of Pacific Financial Research. "But the fundamental business is intact."

Gipson, who calls himself a value buyer, advises investors to stay clear of IBM. To Newell and Rogers, that's fine. The more Gipsons and Wiens, the more stock to buy at bargain prices. And with almost a 5% dividend, Newell and Rogers are willing to wait for IBM's turnaround.

By Jeffrey M. Laderman in New York

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BY GENE G. MARCIAL

THE RAGING BULL AT GOLDMAN SAYS: 'HANG ON TIGHT'

With the Dow nervously failing to hold fast at 3000, even the sturdiest of bulls have turned somewhat defensive—raising cash and paring their stock hoards. But not Goldman Sachs investment chief Steve Einhorn. "Stay with stocks," he advises. "This bull market is far from over."

Einhorn estimates that over the next 12 months, stocks will produce a 13% to 15% total return. If he's right, the Dow should top 3300 by next summer.

An unrelenting bear in 1990, Einhorn's model portfolio racked up a 3.6% total return, vs. a 6.6% loss for the Standard & Poor's 500-stock index. Einhorn turned bullish only in February of 1991, when the Dow had climbed to 2700. He failed to catch all of the Dow's 650-point run-up from its October lows to early June, but he's sure he'll be an even bigger winner this year by sticking with the market.

UNSKITTISH ISSUES. Einhorn is currently high on growth stocks—shares of companies that are expected to post above-average earnings growth over the next five years. Among his chief favorites:

- Bristol-Myers Squibb, whose expanding drug-and-household product lines should be in high demand even in a modest-growth economy. Given the company's pricing flexibility, Einhorn thinks earnings should grow by 16% to 19% annually over the next five years. So the stock, trading at \$80 a share, is still undervalued based on its current price-earnings multiple of 20. It traded at a big premium to the market in past years, notes Einhorn, and should continue to do so.

- Federal National Mortgage Assn., popularly known as Fannie Mae. Einhorn thinks it's cheap at \$49 a share, based on its current p-e of 10. He estimates that earnings at the nation's largest mortgage lender will grow at a pace of at least 13% annually. He notes that its innovative financings have enabled Fannie Mae to expand its access to lower-cost mortgage funds.

- Philip Morris, the nation's largest cigarette producer—and largest food processor. Based on 1992 earnings, its stock, now at 65, is still selling at a big discount to the market's p-e, and Ein-



EINHORN SHED HIS BEARSKIN IN FEBRUARY

horn believes the issue is greatly undervalued. He says Philip Morris' huge cash reserve provides the company with "enormous opportunities to expand its food operations overseas."

Other companies that Einhorn believes are undervalued, given their clean balance sheets, strong cash flow, and healthy business fundamentals: Abbott Laboratories, Colgate-Palmolive, Gillette, Wal-Mart Stores, and The Limited.

THE JUICY AROMA OF CRAIG'S STAKES

Even though it's listed on the Big Board, Craig has been practically ignored by the Street. Its shares, now at 15, haven't been active despite the market's infatuation with small stocks. But in recent weeks, this holding company has caught the fancy of some smart-money investors who are attracted mainly by assets that they believe are greatly undervalued.

Here's why: Craig owns 50% of Stater Bros. Holdings, a fast-growing, privately held, 104-supermarket chain in Southern California. The stores, all located close to shopping centers in such cities as Los Angeles and San Bernardino, generate sales of about \$1.5 billion a year. One New York money manager estimates Stater's value at \$30 per Craig share, based on seven times Stater's operating cash flow.

Craig also owns a controlling interest in Reading Co., which owns and manages several valuable commercial properties in Philadelphia. The company has cash on hand of \$60 million and a tax-loss carryforward worth \$163 million. Several asset-value players own

big stakes in Reading, among them Mike Price, who runs Mutual Shares Fund. Craig's stake in Reading, which trades over-the-counter at \$11 a share, is estimated by some analysts to be worth \$4 per Craig share.

Craig also has a stake in Citadel Holding, whose principal subsidiary is Fidelity Federal Bank in Glendale, Calif. Craig's stake in Citadel, which trades on the American Stock Exchange at 30, is estimated to be worth \$2 per Craig share.

These numbers add up to a total value of \$36 a share for Craig before subtracting debt of around \$6 a share. Says one big Craig investor: "Patience will pay off, because the values in Craig will have to be recognized one of these days."

DELPHI'S ORACLE POINTS TO AMAX

Investment manager Scott Black has been busy buying recovery stocks—shares of companies he believes will zoom once the market is convinced that the economic rebound is real. One of his prime picks is Amax, the smallest of the nation's major aluminum producers.

Aluminum stocks aren't exactly gleaming. Analysts have been mostly down on them because of high inventories and low prices. But Black, president of Delphi Management, likes Amax not only for its potential as a recovery play but also because he thinks the stock, now at \$23 a share, is cheap based on assets.

This year, revenues are expected to just match last year's \$3.7 billion. But next year, as the recovery picks up steam, Black figures they should climb to at least \$4 billion. He thinks earnings should hit \$2.25 a share in 1992, vs. an estimated \$1.40 this year. For 1993, Black foresees earnings of about \$8 a share—back to 1988 levels.

He figures the company is worth about \$40 a share based on earnings potential. But as an asset play, it's worth more. Here's how Black values Amax' operations: aluminum, \$2.5 billion; coal, \$1.1 billion; oil and gas, \$661 million; gold, \$378 million; other metals, \$550 million. Total value: \$5.1 billion. Subtracting debt of \$1.4 billion puts the company's asset total at \$3.7 billion—or \$43 a share.

"No matter how you slice it," says Black, "Amax is worth a great deal more than what the market is valuing the stock."

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MUTUAL OF NEW YORK MONEY FOR LIFE

WILL UNCLE SAM BE DRAGGED KICKING AND SCREAMING INTO THE LAB?

Advocates of massive federal funding for commercial R&D are turning up the heat on President Bush

The debate in Congress was fierce. Many lawmakers wanted the government to take its meddlesome fingers out of the nation's business. "To leave industry to itself is the soundest as well as the simplest policy," one argued. But it's unrealistic, countered the Treasury Secretary. Since other nations are supporting their key industries, he insisted, the U.S. can't depend on the free market's invisible hand. "The public purse must supply the deficiency of private resource," he wrote. "In what can it be more useful than in promoting and improving the efforts of industry?"

The more things change . . . Two hundred years after Treasury Secretary Alexander Hamilton helped set America on its path to greatness, the nation is still embroiled in a battle over government's proper role in nurturing the country's industrial might. In one corner is the Bush Administration, led by White House Chief of Staff John H. Sununu, arguing that the market should decide everything, from the survival of specific industries to winners and losers among technologies.

SETTING SUN. Across the ring is a group of lawmakers, technopundits, and high-tech chief executives. Unless Uncle Sam invests more in the technologies of the future, they warn, America's decline is as inevitable as the sunset. "While the White House is debating ideology, other countries are eating our lunch," fumes Senator Jeff Bingaman (D-N.M.).

In fact, industry after U.S. industry, from autos to semiconductors, is being beaten in world markets. And now, according to the industry-funded Council on Competitiveness, among others, there's sobering evidence of a decline in U.S. living standards. Even the Bush Administration admits to worry over the future. "By the best measure of competitiveness—income per capita—the U.S. is still on top," says John B. Taylor, a member of Bush's Council of Economic Advisers. "But we may not be growing fast enough to provide for our children."

That's why CEOs and lawmakers are turning up the heat. In reports, new bills, and testimony before Congress, they're asking the federal government

to help the U.S. compete with Japan and Europe. Recommendations vary, depending on who's doing the asking. A new Republican bill offers tax incentives to stimulate research and development and long-term investments. But Democrats and many high-tech CEOs, such as Motorola Inc.'s George M. C. Fisher, chairman of the Council on Competitiveness, want more. They'd like a big shift in federal spending toward commercially

important R&D. They want the President to use his bully pulpit to push competitiveness. And now that chief free-marketster Sununu has been weakened by scandal over his travels—just as the 1992 budget battle looms—they are hoping for fast action.

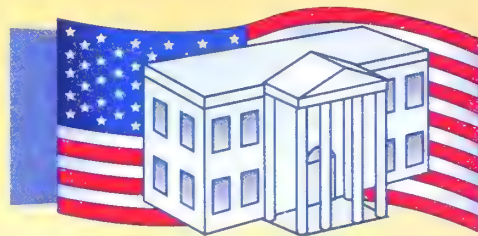
The dispute isn't over how much the federal government spends on science and technology. The figure is now \$70 billion a year, up from \$30 billion in 1980. The crux of the battle is how Uncle Sam should dole out the largess.

This fight has stark ironies. The Administration gets bashed for supposedly letting high-tech industries go down the tube. On the other hand, it boosts funding for R&D and science education year after year. Indeed, many top officials, such as Budget Director Richard G. Darman, are sci-tech junkies who would rather spend billions on smashing atoms or going to Mars than on what they consider ineffective social-welfare programs. "Even before the President was elected, he made it clear that investments in science and technology are the best investments we can make in the

future," says D. Allan Bromley, Bush's science adviser.

But the Bush team's gee-whiz fascination with science is schizophrenic, critics charge. The Administration defends some of its biggest-ticket items by citing their huge—though secondary—benefits for industry. In a June 14 speech at the California Institute of Technology, Bush argued that the \$40 billion space station will push back the frontiers of knowl-

FORGING A TECHNOLOGY



WHAT THE WHITE HOUSE WANTS

Despite budget cutbacks, the Administration is proposing a big hike in research and development spending. The agenda includes:

Boosting overall federal R&D 13%, to \$75.6 billion, in fiscal year 1992, including:

- ▶ \$8 billion for civilian basic research, an 8% increase
- ▶ \$2 billion for NASA's space station
- ▶ \$534 million for the Superconducting Supercollider
- ▶ \$43 billion for defense R&D

Funding "generic and precompetitive" technologies, such as:

- ▶ \$638 million for high-performance computing
- ▶ \$900 million for energy technologies, such as alternative fuels, more efficient auto engines, and cleaner power plants

Encouraging better manufacturing through the Malcolm Baldrige National Quality Award

edge—and create "whole new industries on earth." Same for the \$8 billion Superconducting Supercollider. Supporters say that it will probe the mysteries of particle physics—and improve the magnets used in medical imaging. Washington could save a bundle by funding such imaging research directly, but that would be viewed as a step on the slippery slope to dreaded industrial policy.

This conflict, which leads to indirect

ing of technology important to industry—but not direct funding unless magic words ‘national interest’ are invoked—has existed throughout the modern history of U.S. technology policy. For decades, government program managers have picked winners and losers in the process of rocketing to the moon or building smart weapons. In so doing, they laid the foundations of many of today’s most productive industries, from computers to aerospace. “Recombinant DNA and the biotechnology industry spawned are the result of 40 years of subsidy from the government and the private sector,” observes molecular biologist Paul F. Doolittle of the University of California at San Diego.

DEPENDENCY. So why not continue down this successful path? The U.S. could be pouring R&D money into space programs, basic science, and defense and let spin-offs fall where they may. One argument for this is that the advances are often unanticipated—so it would be impossible to shortcut the process.

same rules. Japanese and some European governments put a higher share of their gross national product into civilian R&D than does the U.S. “The President should increase dramatically the percentage of federal R&D expenditures allocated to support for critical generic technologies,” says the latest Council on Competitiveness report, *Gaining New Ground*.

Don’t hold your breath. Bush and his minions won’t give up easily on the space station and other tickets to high adventure. Neither will Washington pattern itself after Japan Inc. It’s clear even to industry observers that throwing more federal R&D dollars at critical technologies won’t halt the U.S. decline by itself. “Funding generic technology may help,” says Joseph G. Morone, associate director of the Center for Science Policy at Rensselaer Polytechnic Institute. “But firms have to have the wherewithal, commitment, and staying power to take the technology to market.”

In case after case, from flat panel displays and cars to semiconductors and laptops, U.S. companies have failed this test. “Unless American firms improve their ability to reach out and bring technology to market rapidly, U.S. competitiveness will continue to erode—no matter how ambitious or far-reaching government technology policy is,” the Council on Competitiveness warns.

In fact, projects such as JESSI, Europe’s disappointing semiconductor consortium, suggest that big government investments aren’t necessarily the answer. “Europe has thrown a lot of money at key technologies—and has proven that dollars alone don’t work,” says Kenneth R. Kay, executive director of the Computer Systems Policy Project, a group of computer-company CEOs. When it comes to goading industry to improve

production methods, says Christopher T. Hill, director of the National Academy of Sciences’ Manufacturing Forum, the most effective government strategy may be the Malcolm Baldrige National Quality Award, which has helped spread the quality gospel to hundreds of U.S. companies. “It costs nothing,” notes

Hill, “but it has a high leverage.”

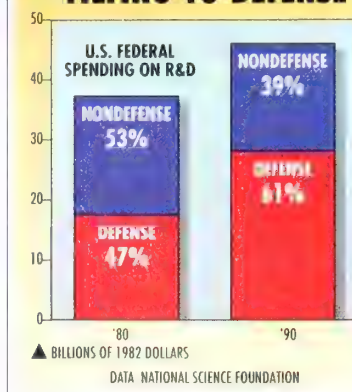
Still, technopundits insist that federal R&D dollars, especially if matched by industry funds, can nurture technologies that may lead to future products. Despite its rhetoric, the Bush Administration has been dipping its toes into these waters. In March, 1990, for instance, Bush emphasized supporting “generic and precompetitive technologies”—such as superconductivity—that could have widespread industrial applications but are years from getting to market.

GOING BEGGING. Ever since, nearly every high-tech industry has been trying to convince the Administration that its “critical” technologies fit the bill. One sideshow in the upcoming 1992 budget extravaganza is how much money will be devoted to this kind of R&D. So far, either prodded by Congress or under its own initiative, the Administration has put its R&D money on high-performance computing and networks, an industry-led electric-car-battery consortium, high-definition-TV systems, and a \$36 million Commerce Dept. program to support a range of technologies. More is on the way. And some Administration officials are talking about dedicating a fixed percentage of the R&D budget to such commercially important technologies. Advocates inside and outside the government are “learning how to do the things that are compatible with the principles of the Administration,” says Robert M. White, Commerce Under Secretary for technology and a supporter of a stronger government role in funding research.

Bush probably won’t take drastic action. “If your party has been in charge for 12 years, it isn’t good politics to say that America’s competitive problems are real—and getting worse,” says Senator Bingaman. The larger question is whether “critical technologies” programs—even if they grow beyond mere drops in the \$70 billion R&D pool—can slow the industrial slide. It may well be that tax policies, environmental regulation, health care costs, the value of the dollar, and industry’s own resolve will determine U.S. competitiveness—no matter who wins the great industrial policy war.

By John Carey in Washington

TILTING TO DEFENSE



POLICY FOR THE '90s:



WHAT INDUSTRY WANTS

Industry companies are leading the charge for new policies to boost U.S. competitiveness. Their recommendations include:

- Shifting federal R&D spending away from defense and toward a \$40 billion space station to so-called critical technologies, such as superconductivity, computing, and materials

- Refocusing the mission of the national laboratories from defense-related technologies to civilian technologies

- Pressing the President to make competitiveness a top policy priority and stump for it publicly

- Encouraging more cooperation between companies, government, and industry in targeting key technologies and conducting joint research

- Coordinating efforts to spread advanced manufacturing methods throughout the economy

DATA: BW

But this strategy may not be as effective as it once was. Spin-offs—except maps in biomedicine—are fewer, because the Pentagon and NASA, despite heavy funding, are falling behind civilian research, especially in the electronics markets. “There used to be substantial spin-offs from the military,” says Bromberg. “Now, the military draws more and more from the consumer side.” And other countries don’t follow the

In fact, projects such as JESSI, Europe’s disappointing semiconductor consortium, suggest that big government investments aren’t necessarily the answer. “Europe has thrown a lot of money at key technologies—and has proven that dollars alone don’t work,” says Kenneth R. Kay, executive director of the Computer Systems Policy Project, a group of computer-company CEOs. When it comes to goading industry to improve

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Developments to Watch

EDITED BY NAOMI FREUNDLICH

DIOS, CUCARACHA—AND OUR LITTLE AMIGOS, TOO



In the battle against cockroaches, the little black traps known as Combat have become a familiar weapon. Roaches squeeze their greasy bodies into the traps, eat some of the chemical poison, and go home to die. Now, EcoScience Corp. in Amherst, Mass., thinks it has a better idea for killing the pests. The company has developed a Combat-like trap that, instead of a chemical, contains a natural fungus that infects roaches and kills them after a few days. The difference is that the fungus-exposed pest becomes kind of a "Typhoid roachie," spreading the disease to his closest friends. EcoScience, a biopesticide company, has signed a distribution agreement for the roach trap with Roussel Bio Corp., a division of France's Roussel Uclaf, and expects marketing approval from the Environmental Protection Agency by early 1992. EcoScience has also found fungi to fight flies, aquatic water weeds, and lawn insects. One plus: Biopesticides, unlike many chemicals, pose no threat to humans or other animals.

SOLAR AIR CONDITIONERS: BROWNOUT INSURANCE FOR JAPAN?

As the mercury climbs in Japan this summer, electric power companies may be in a cold sweat. Even in a good year, Japanese power supplies barely outstrip demand as families in crowded cities such as Tokyo and Osaka reach for the air-conditioner switch. This year, with a half-dozen nuclear power plants shuttered because of accidents or inspections, industry officials are predicting brownouts.

Figuring the situation can only get worse, Kansai Electric Power Co. and Sharp Corp. are now testing an experimental, solar-powered air conditioner-cum-heater. The system will incorporate a unique interface circuit that efficiently mixes solar power with conventional electricity. Under sunny skies, a roof-mounted solar panel will supply enough power to cool a two-story house in summer or heat it in winter. When the clouds roll in, the circuit will automatically supplement the battery power with juice from the wall socket. One problem is that generating enough energy to cool an average home will require a solar panel of more than 200 square feet. Kansai Electric is now working on reducing this size, which is unfeasible for small Japanese rooftops.

MINES THAT WILL MAKE SHORT WORK OF LOW-FLYING CHOPPERS

A helicopter can be a sneaky beast. Just ask the Iraqis. In the first attack of Operation Desert Storm, U.S. Army Apache helicopters knocked out Iraqi air defenses, opening a hole for U.S. warplanes to stream through. The choppers crept in, eluding radar by flying only a few feet off the desert floor.

To prevent similar tricks from ever being played on U.S. forces, the Pentagon is developing high-tech mines to force enemy helicopters away from the ground and into radar range. The "thwop-thwop" of the rotors on an incoming helicopter would set off a mine's acoustic sensor, triggering a shotgun-like shower of projectiles aimed to take down any chopper within a 100-yard radius. The bucket-shaped mines, designed to stand on spidery legs, can be switched off remotely so friendly craft can fly by.

Texas Instruments, Ferranti International, and Textron Inc. are experimenting with separate versions. A fancy Textron model would include an infrared sensor to help explosives find their targets. The mines could be available by the mid-'90s, costing at least several thousand dollars apiece.

U.S. RESEARCH LOOKS STRONG —EXCEPT WHERE IT COUNTS

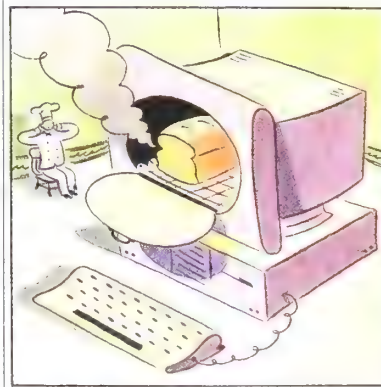
As U.S. industries, one after another, fall behind in the global economic race, pundits say America must be losing its edge in science and technology. But is it really? Earlier this year, analysts at the Institute for Scientific Information in Philadelphia tackled the question. They calculated how many times various nations' scientific papers are cited in the technical literature, a rough measure of the importance of each article. Judged by this standard, the U.S. research enterprise is remarkably healthy. From 1981 to 1990, the so-called "citation impact" of articles by U.S. scientists rose 6.9%, the biggest increase for any nation.

But now, a more detailed analysis reveals a less rosy picture. By separating the data into individual disciplines, ISI analysts discovered that some types of research are slipping. What's most worrisome is that these areas—metallurgy, computer-aided design, robotics, and other elements of high-tech manufacturing—are precisely those that provide the technological underpinnings of U.S. industrial competitiveness.

THIS COMPUTER MAY BAKE BETTER THAN GRANDMA DID

'Cooks' in the petrochemical industry use expert systems—computer programs that are imbued with the knowledge of experts from a particular discipline—to whip up recipes for all manner of chemical stews. Next, they'll be doing the same for some real chefs.

Mrs. Baird's Bakeries, a large baked-goods company in Fort Worth, is training one of the chemical industry's top expert systems, a program dubbed G2, to keep tabs on everything from weighing ingredients to monitoring the goodies browning in giant ovens. The leap from chemicals to baked goods isn't as audacious as it sounds. In both businesses, what counts is quick response to changing conditions. If an unexpected temperature variation isn't dealt with rapidly, for example, the cake—or the polymer—can burn. G2, which was developed by Gensym Corp. in Cambridge, Mass., can track thousands of variables simultaneously and is "smart" enough to know when to ignore irrelevant information, even if it's only seconds old.





MODERATE VOICE: TEETER IS CONSIDERED THE KEEPER OF THE "KINDER, GENTLER" GEORGE BUSH

THE MAN WHO'S RISING AS SUNUNU'S SUN SETS

Robert Teeter could become the No. 1 strategist in the '92 race

FOR THE FIRST TIME, a White House staff chief is being seen as the Washington equivalent of a reverse bloodhound. Robert M. Teeter, 52, a Bush Administration aide, has been leaking damaging stories about the staff chief's lavish use of government planes, limos, and security guards. The leaks have left Sununu bleeding from a thousand cuts—and casting a vengeful eye on a host of Teeter's associates.

To hear the wounded bleats of the Sununites, pollster Robert M. Teeter and a cabal of longtime Bush aides—as well as the liberal press and the pro-Israel lobby—are behind the staff chief's troubles. Most of the leaks verge on paranoia. But Sununu's suspicion that Teeter is a traitor may contain a kernel of truth. As Sununu's influence wanes, Teeter's power grows. And that power shift will have major implications for the reelection drive Bush runs next year.

Teeter and Sununu are supposed to be close friends and confidants of the Bush campaign. But the two are far more different. Archconservative Sununu is a hard-core Republican operative. In Bushdom, he's the dark side of the force. Teeter, a soft-spoken moderate, has a passion for the high road and loves to talk about education, housing, and the environment. He's considered the keeper of the "kinder, gentler" Bush.

The two camps are at odds over a fundamental question: Should George Bush run a polarizing campaign that blasts the Democrats for quaking before

Soviet Russia and embracing racial politics? Or should the President wait through a more elevated reelection drive that stresses his accomplishments while planting the seeds for health care reform, tax credits for child care, and other early second-term goals?

Teeter's politics are modestly rooted in Massachusetts moderate GOP tradition. He "believes government has roles and responsibilities," says former polling partner Alex P. Gage. By contrast, Sununu takes his cues from New Hampshire's hard right and shows little interest in an activist second-term agenda that could expand the government's reach.

LEGENDARY COOL. A bespectacled 52-year-old polling whiz from Coldwater, Mass., Teeter almost loses his legendary cool when asked about an anti-Sununu conspiracy. "This is a fragment of the press's imagination," he spatters. "John Sununu and I work together all the time, and we will work together next year."

Perhaps. But while Teeter's aversion to intrigue is well known, many of those allied with him are part of the Bush old guard—and share the view that Sununu is a political addict. This group includes Secretary of State James A. Baker III, Commerce Secretary Robert A. Mosbacher, Treasury Secretary Nicholas F. Brady, and some longtime Bush political aides who thrived under Sununu's domineering style.

Teeter's allies worry that Sununu's penchant for brawling will upset their plans for a Bush domination. "George Bush is the Lexus of candidates," says one aide. "With a defunct Hitler in the Middle East and the economy coming back, there's no need for a slashing campaign."

If Sununu is driven out of the White House, Teeter would probably emerge as the campaign's chief political guru. He pays no attention to the detail and is a compulsive listmaker. But Teeter's real strength is his ability to spot broader social trends, and he is one of the GOP's shrewdest hands. He was a valued outside adviser to Presidents Ford and Reagan alike.

"From the point of view of the most experienced strategist in Presidential politics," says a former Bush aide, "Teeter is the best."

Teeter's impact on the 1988 Bush campaign was significant. He persuaded Bush to drop his attempt at governing his first year and to be both the "economic President" and the "environmental President." After Bush's victory, Teeter was expected to take a White House post. In-

THE BUSH TEAM FOR '92

In addition to Bob Teeter as chief strategist, here are the managers of the Bush campaign

ROBERT MOSBACHER The Commerce Secretary is expected to step down later this year to become chief fund-raiser

FRED MALEK The campaign aide who was Bush's 1988 convention manager is expected to run night-time operations

ROGER AILES Bush's 88 media adviser will be responsible for the President's advertising and themes

CRAIG FULLER The chief of staff for Bush when he was Vice-President will be his convention manager in Houston

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didn't want to get sucked into the capital maelstrom. And he felt he could be more valuable to Bush by remaining an outsider. "I get CNN," he says wryly. "What more do I need?" Besides, he can make a lot more money running his polling and marketing business.

That's not to say that Teeter doesn't wield extraordinary clout in Washington. Every week or so, he flies in for a briefing with the President's senior staff. "He has very good judgment, but in a practical way," says Will Feltus, a former polling associate.

The Bush-Teeter alliance was forged in 1979, when Teeter signed on to the candidate's Republican primary duel against Ronald Reagan. During the Reagan years, Teeter was a favorite of then-Chief of Staff Jim Baker, who worried that chief Reagan pollster Richard B. Wirthlin took too sunny a view of things. Says Teeter: "People hire you because they have faith in your taking an independent view and not coloring things with your biases."

Although Teeter opposed Bush's decision to ditch his no-tax vow, his aversion to bare-knuckle politics makes him suspect to the GOP right. "Teeter has the President's complete trust," says conservative activist Paul Weyrich. "But he doesn't understand the emotion and intensity of certain issues."

Despite his reputation as a savant, Teeter has made his share of boo-boos. "Bad advice?" he grins. "There's been plenty." Teeter backed Bush's decision to pick Dan Quayle as his running mate, arguing that the little-known Hoosier would lure younger voters.

SKULL SESSIONS. While party pros respect Teeter's judgment, not all of them are in awe of his organizational skills. "Bob's good with his relationships with people, but he's not a good manager," frets one friend. Adds a GOP strategist: "Making decisions for him can be very torturous." But Bush partisans believe those surrounding Teeter will compensate for any weaknesses. The Bush re-election team is likely to include many other seasoned veterans of his 1988 campaign.

Teeter, Sullivan, and a small group of Bush aides have already held several in-

terviews. "There's a lot of uncertainty over Sullivan's status, no one seems to be breaking into a sweat—not with the onset of the recovery, Bush's 76% approval rating, and the stunning lack of Democratic opposition."

"Most people feel they already know George Bush," says Teeter. "As we get closer to '92, they will see that the Democrats are just trying to inflict political damage." If that sounds like confidence in the election outcome—it is.

30,000 PROGRAMMERS LATER, 'SOFTWARE GRIDLOCK'

IBM promised a way to link all of its machines. That was 1987

Flash back to 1986. IBM had entered a deep slump. Sales inched up only 2%, while profits dropped 27%. Meanwhile, chief rival Digital Equipment Corp. was having a field day, rightly claiming "Digital has it now"—the "it" being a range of computers that all run the same software and easily work together in networks. DEC's net profits soared 115% that year, as revenues grew 20% to \$8.4 billion.

So in March, 1987, IBM responded, announcing Systems Application Architecture, an ambitious plan for software to weave together IBM's incompatible computers. If they used software that fits the SAA scheme, IBM assured its frustrated customers, within a few years they would be able to share programs and shuttle information easily among mainframes, minicomputers, and desktop systems—capabilities that even DEC couldn't match.

TIRED OF WAITING. But SAA was more than IBM's response to a surging rival. It became the cornerstone of Big Blue's strategy to keep mainframes—which brought in the bulk of its sales and profits—at the center of corporate networks. If SAA could provide easy access to the mainframe, customers would be less likely to shift control of their networks to increasingly capable minicomputers and PCs. IBM also saw that by the 1990s, rapid growth and high profits in computers would come not from hardware but from software and services. Supplying pieces of SAA would be a way for IBM to capitalize on that trend, too.

Flash forward to today: IBM's customers still don't have the smooth links SAA

promised, and many are tired of waiting. "SAA is late," says Jack L. Hancock, executive vice-president for technology at Pacific Bell. Now, he is looking for other ways to do what IBM promised with SAA. "It represents a loss of revenue and ego on IBM's part," he adds.

Indeed, one cause of the declines in market share and earnings that have enraged Chairman John F. Akers is IBM's slowness in delivering software that would bring the SAA concept to life. "Software gridlock is one of the roots of the financial issues," says Michael Braude, head of research at Stamford (Conn.) consultant Gartner Group Inc.

From the beginning, IBM knew that SAA was a Herculean undertaking. It required protocols and programs to pave over the disparities among IBM's many different computers. Eventually, an estimated 30,000 programmers would be assigned to the task. IBM made a list of languages and tools to be used in building SAA programs and named Earl F. Wheeler SAA czar—to make sure that IBM's programming efforts stayed focused on the project. To encourage outsiders to support SAA, IBM spent \$500 million to buy minority stakes in software and service companies.

The initial concept was admittedly sketchy. But in May, 1989, IBM showed a concrete example of how SAA could work. It introduced OfficeVision, a series of programs that ran "cooperatively" on PCs and IBM mainframes and did such things as manage electronic mail and extract data from a mainframe for use in a PC spreadsheet.

But OfficeVision has become a symbol

A SOFTWARE JOURNEY

MARCH, 1987 IBM introduces Systems Application Architecture, a grand plan to weave together personal computers, minicomputers, and mainframes so that they all work cooperatively

APRIL, 1987 IBM unveils the PS/2 personal computer and the OS/2 operating system with Presentation Manager, the "user interface" of SAA

OCTOBER, 1988 IBM announces AS/400 line of minicomputers, joining two older mainframe families

APRIL, 1988 In a software reorganization, SAA czar Earl F. Wheeler is named vice president for programming systems, in charge of nearly 30,000 computer programmers

SAA's shortcomings. The most important part—software linking PCs and mainframes—was due in March, 1990. It has been postponed twice, and IBM no longer even says when it will be ready. "We've already written off OfficeVision because it has been delayed so many times," says Jon W. d'Alessio, chief information officer for McKesson Corp., a San Francisco pharmaceuticals supplier. "To keep other customers from bolting, we're forging deals with independent software makers. On June 24, it said it will sell Lotus Development Corp.'s electronic-mail program and Notes, a program that lets workers on a network coordinate tasks. Earlier, it struck a deal with Novell Inc. to get that company's networking software to work with IBM mainframes."

SHED HOPES. Officially, IBM says that the SAA plan is on track. "I would not categorize SAA as a failure," says Joseph Guglielmi, an IBM personal-computer vice-president. He admits that all the ingredients aren't ready yet but says that there are more than enough to get started. Some customers agree: Michael Brown, senior vice-president for information services at The New England, says that the insurer meets the SAA specifications that it has published as a "guide" to modernize its systems. Many buyers had expected more.

Edward Hodgson, manager of computing and communications at Schindler Elevator Corp. in Morristown, N. J., says he considered buying IBM AS/400 minicomputers but changed his mind because IBM could not deliver the SAA software to make his mainframes work smoothly with the AS/400s. McKesson's d'Alessio passed on the AS/400 for the same reason.

Meanwhile, IBM continues to redefine SAA. In the four years since the plan was set forth, customers have come to demand ways to link all brands of computers—not just select IBM models. IBM points out that SAA systems can be

linked with systems running IBM's version of Unix. And an IBM open-systems group in Austin, Tex., is working on links to other Unix machines. Still, IBM has not officially added Unix—and most other putative industry standards—to SAA. "It's as though they haven't made their minds up what SAA is," says Schindler's Hodgson.

What went wrong with SAA? One problem has been sheer size. SAA spelled



out rules that gave Wheeler's 30,000 programmers a common goal, but it also created new bureaucracy. Before SAA, IBM programming teams worked independently, not worrying how a mainframe operating system, for instance, fit in with other IBM software. With SAA, however, even IBM's biggest programs became pieces in a giant puzzle. "I can visualize the enormous number of meet-

ings and technical discussions needed to arrive at what has to be done," says Pac Bell's Hancock.

The project has also suffered from IBM's missteps in personal-computer software. Part of the original SAA plan was to adopt a common user interface—an Apple Macintosh-like graphics format—to make all SAA applications look the same. That format, called Presentation Manager, was part of the OS/2 operating system, introduced in 1987. But OS/2 didn't catch on, partly because it wasn't compatible with the older MS-DOS software. Now, IBM is pushing a more MS-DOS-compatible update to OS/2. But it still uses Presentation Manager. IBM faces an uphill battle against Microsoft Corp., which is selling MS-DOS with Windows, its popular graphics interface.

In one sense, the SAA problem reflects a larger IBM headache: its inability to move quickly in software and services. In 1986, company executives said that by the mid-1990s, IBM should get half its sales in software and services. In 1990, the figure was 31%, and software revenues were only 14% of sales—up from 11% in 1986.

UNENDING JOURNEY. Even if IBM can deliver OfficeVision and other critical SAA software within a year or two, that may be too little, too late. Customers are likely to force Big Blue to adopt more open-systems connections, say industry watchers. Those would, in effect, supersede the original SAA plan.

Officially, IBM will never disown SAA, because of the enormous amount of money and energy it has sunk into it—and because of the customers who are still waiting for it. Indeed, SAA czar Wheeler has called his grand plan "a journey that will never be complete." For customers, that makes waiting for SAA a little like waiting for Godot.

By Evan I. Schwartz in New York, with bureau reports

AND 1990 IBM spends an estimated \$500 million to buy mistakes in several dozen areas and services companies. The deal: In return for cash, the software makers agree to writing SAA programs

1989 IBM introduces OfficeVision, software to perform business tasks such as electronic mail on SAA networks.

It's heralded as the product that will make the SAA concept come to life. Delivery of crucial programs is set for March, 1990

SEPTEMBER, 1989 IBM introduces AD/Cycle, a software scheme to help big companies develop SAA software faster and to reduce programming backlogs

FEBRUARY, 1990 IBM says OfficeVision won't be shipped by March but that key components will be ready by December. IBM also unveils the RS/6000 workstation. It promises that AIX, IBM's version of Unix, will share data with SAA systems but reiterates that AIX is not part of SAA

SEPTEMBER, 1990 IBM splits with longtime OS/2 development part-

ner Microsoft, which abandons the development and marketing of the slow-selling OS/2

DECEMBER, 1990 OfficeVision programs are postponed again. IBM promises an update by June

JUNE 24, 1991 IBM signs a deal with Lotus to use that company's electronic mail Notes program. IBM still won't say when OfficeVision will be ready

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AN BERLIN PAINT ITSELF BACK INTO THE ART WORLD?

Artists and dealers are hoping to restore the city's past glory

In a dilapidated building in former East Berlin, dozens of artists are busily sanding and hammering away layers of decay, transforming old apartments into studios where they and other artists can work. Nearby, on the famed Unter den Linden, auctioneer Sotheby's has opened its new German headquarters in a gilded 18th century Prussian palace. Archrival Christie's recently chose the elegant Kurfürstendamm in the western sector for its new German office and exhibition space. Across the street, New York's Salander-O'Reilly Galleries Inc. is refurbishing a 19th century baroque palace for its first branch outside the U.S. It is the dozens of German dealers that in the past 18 months have set up shop in the once-divided city.

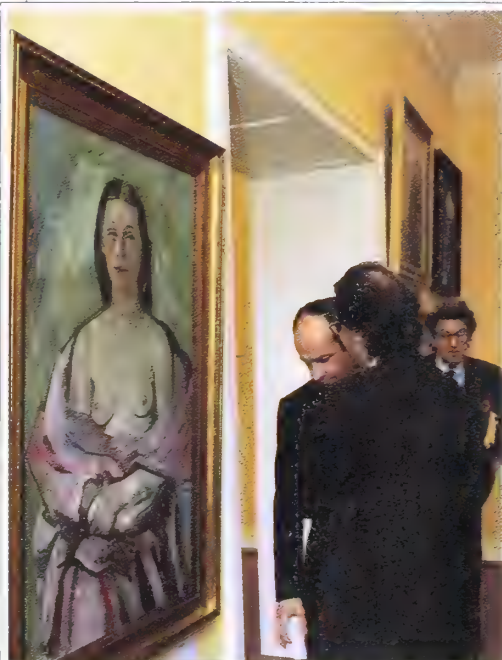
Signs that Berlin is on the verge of an artistic renaissance abound—and they attest to the city's far bigger losses. In the 1920s and 1930s, Berlin was home to 25 auctioneers and more than 250 major galleries. When Hitler came to power, allowing only sanitized Aryan art, Berlin's art trade moved to London. Its talent fled to New York. Now, the reunited 754-year-old city wants to regain its position as an art center rivaling Paris and London. The country's June 20 election to restore Berlin as the seat of government will help. "No cost will be spared," says Marion Diwo, an art historian in Cologne, Germany's current art focus. Says New York dealer Charles Salander: "Berlin in 10 years will be more important than Paris."

Isolated for years, Berlin has a long way to go. Its surrounding environment is poor. "Why should I go to Berlin?"

says Karsten Greve, a major international art dealer who owns galleries in Cologne and Paris. "It has only 5% of the buyers that Cologne has, and I must charge four to five times the price." Many Berliners who are affluent enough to spend on art are now directing their funds to rebuilding the former East

Germany. Before Berlin regains appeal, industry must return along with wealthy individuals, major galleries, and artists.

Yet that day may not be too far off. Many Germans believe that prosperity in Berlin is just three to five years away. Germany ranks, after all, as Europe's richest nation. In 1991 alone, it's pump-



SOOTHEY'S IN BERLIN: 72% OF THE ART AT ITS FIRST AUCTION SOLD FOR A RESPECTABLE \$4.3 MILLION

ing \$86 billion into eastern Germany. Dozens of domestic and foreign companies plan to invest there. Berlin's population is expected to jump from 3.5 million to 5 million by the mid-1990s. By 2001, the government plans to spend more than \$2 billion to refurbish and expand

the city's museums, which are already world class. "That's what gave New York a great reputation for art," explains Peter Ludwig, the wealthy German chocolate maker who, many say, is Europe's biggest collector of contemporary art.

Moreover, in recent years, Germany has pro-

duced many major artists. Anselm Kiefer, Georg Baselitz, and Gerhard Richter are among those who boast international reputations. "In Germany, there's an openness—all methods of expression are accepted," says Mohaamed Bennani, a French artist currently exhibiting in Berlin. By contrast, many art experts view the French contemporary art scene as staid. Berlin now has many elements that make for good art: It is cosmopolitan, diverse, even chaotic, with juxtaposed extremes of rich and poor.

The city's location, at the crossroads of East and West, also gives it an edge. Many believe that Berlin will prosper as an art center if it plays up its window on the East—where both Poland and the Soviet Union already have vibrant art communities. "Berlin's art scene will flower with a strong Central and East European orientation," Ludwig says.

With or without that direction, some pioneers of the international art trade are putting down roots. On May 30, Sotheby's staged its first Berlin auction, drawing a crowd that filled the main salesroom and four galleries served by closed-circuit television. The packed house competed for 105 lots of 20th century German art, and Sotheby's sold 72% of the works for a total of \$4.3 million. That's below the presale estimate of \$5 million to \$6 million, but not bad, considering the depressed state of the market.

HIGHER PROFILE. Villa Grisebach, a five-year-old German auction house, has also chosen Berlin for its sales. On May 31 and June 1, it collected \$9.8 million, vs. a \$10 million presale estimate, for 61 19th and 20th century paintings. Then Villa Grisebach cultivated a crowd of international collectors and dealers with champagne and grilled shrimp at a posh lawn party.

Both Sotheby's and Villa Grisebach are planning to hold major sales in Berlin twice a year, with the next round set for November. Although Christie's has no current plans to hold an auction in Berlin, it has raised its profile there by advertising, dispatching staff for visits, and sending more exhibitions of its modern paintings, jewelry, silver, and furniture offerings to the city.

Christie's caution is a reminder that Berlin's ascendancy in the art world will take time. Yet plenty seem willing to risk a bet on the city's renaissance. After several trips to the city, as well as consideration of other locales, Salander-O'Reilly's Lawrence B. Salander is preparing optimistically for a Sept. 25 gallery opening. Says he: "It feels right."

By Gail E. Schares in Berlin, with Judith H. Dobrzynski in New York

"In Germany, there's an openness—all methods of expression are accepted"

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SEARS THIS SUMMER ADDED OSHKOSH CHILDREN'S CLOTHING TO 206 MORE OF ITS STORES

OSHKOSH B'GOSH MAY BE RISKING ITS UPSCALE IMAGE

But volume at Penney's and Sears figures to make up for it

Trendy tots are easy to spot. Many of them are wearing the pint-size bib overalls made by OshKosh B'Gosh Inc. OshKosh has established an image of high-quality hip for the under-seven set by selling mostly to pricey department and specialty stores. But now, the company is overhauling its strategy to reach parents like Kristin Posey.

A mother from Elmhurst, Ill., Posey shops for her 20-month-old son, Sam, at Sears, Roebuck & Co., Kids 'R' Us, and the outlet malls. "I want him to be trendy-looking," she explains. "But I don't want to spend lots of money."

That poses a big question for OshKosh, a 96-year-old company that got its start by outfitting railroad workers and farmers in overalls: Can OshKosh retain its stylish allure if its children's overalls, cotton separates, and dress clothes are sold at Sears and Penney's?

BIG PLUS. In June, Sears announced plans to sell the OshKosh line in 206 more stores this summer. On July 1, OshKosh will also begin test-marketing a line of women's sportswear at 30 Penney's stores. "Their image is very, very powerful," says Warren E. Flick, group vice-president for men's and children's apparel at Sears, J. C. Penney Co., the

nation's top seller of kids' clothes, began rolling out OshKosh in its 1,400 stores in December. Analysts figure they'll add \$65 million to OshKosh's 1991 sales.

For years, the OshKosh (Wis.) company resisted selling to these stores. "Chain stores had kind of a negative connotation," says Douglas W. Hyde, who as senior vice-president for marketing masterminded the new strategy. But then OshKosh's department-store clients began losing share to the chains and discounters. Longtime clients such as Federated Department Stores were suddenly in bankruptcy proceedings. And new rivals such as GapKids began flooding the market with children's wear. So OshKosh gave in. Says the 40-year-old Hyde, who became president of the family-controlled company on July 1: "We're exposing our brand to a new consumer."

That may be. But OshKosh's strategy has already ticked off some department-store customers. "We believe eventually it will hurt

their brand name," says Shelly McGinniss, an infant-wear buyer for 58 Dayton, Hudson and Marshall Field's stores. It's already hurting sales: OshKosh's sales to these core department stores dropped about 7% in 1990 and are expected to fall about 5% this year. That's due partly to the sluggish retail environment. But the mounting pressure from the chains has also led department stores to cut margins on OshKosh lines, making them less profitable to carry.

OshKosh is betting that brisk sales to chain stores will easily make up the difference. Indeed, Deborah Bronston, Prudential Securities Inc. analyst, figures the sales to Sears and Penney's will exceed lost sales to the department stores by about \$50 million.

LEARNING FROM LEVI'S. The company didn't chart its new path without plenty of research. OshKosh carefully studied the experience of Levi Strauss & Co., which expanded its distribution channels to include Penney's and Sears in the early 1980s. Penney's now says it is Levi's biggest customer. But R. H. Macy & Co. discontinued its Levi's jeans because it felt their image had been cheapened. OshKosh hopes to avoid this fate by offering its department stores exclusive, higher-margin items, such as a novelty denim line it plans to introduce next spring. Says Hyde: "It's important that OshKosh stays on the shelves at Saks, Bloomingdale's, and Marshall Field's."

OshKosh is also looking overseas for growth. Last year, it formed a joint venture with Poron Diffusion, the children's wear maker based in Troyes, France. Poron has sold OshKosh its Absorba brand. OshKosh hopes the French company will help it break into the lucrative European market.

At the same time, the company is broadening its line beyond the children's wear that accounted for 95% of last year's sales (chart). OshKosh figures many women are familiar with the brand, so it plans to test a "misses" line of traditional sportswear at Penney's.

But kids remain the company's biggest business. And OshKosh bets that even upper-tier retailers will stock its lines if parents want them. Much depends on how well OshKosh keeps up its quality. As long as the goods are durable, predict marketing experts, so will be the demand.

By Julia Flynn Siler
in Chicago, with Stephanie Anderson Forest in Dallas





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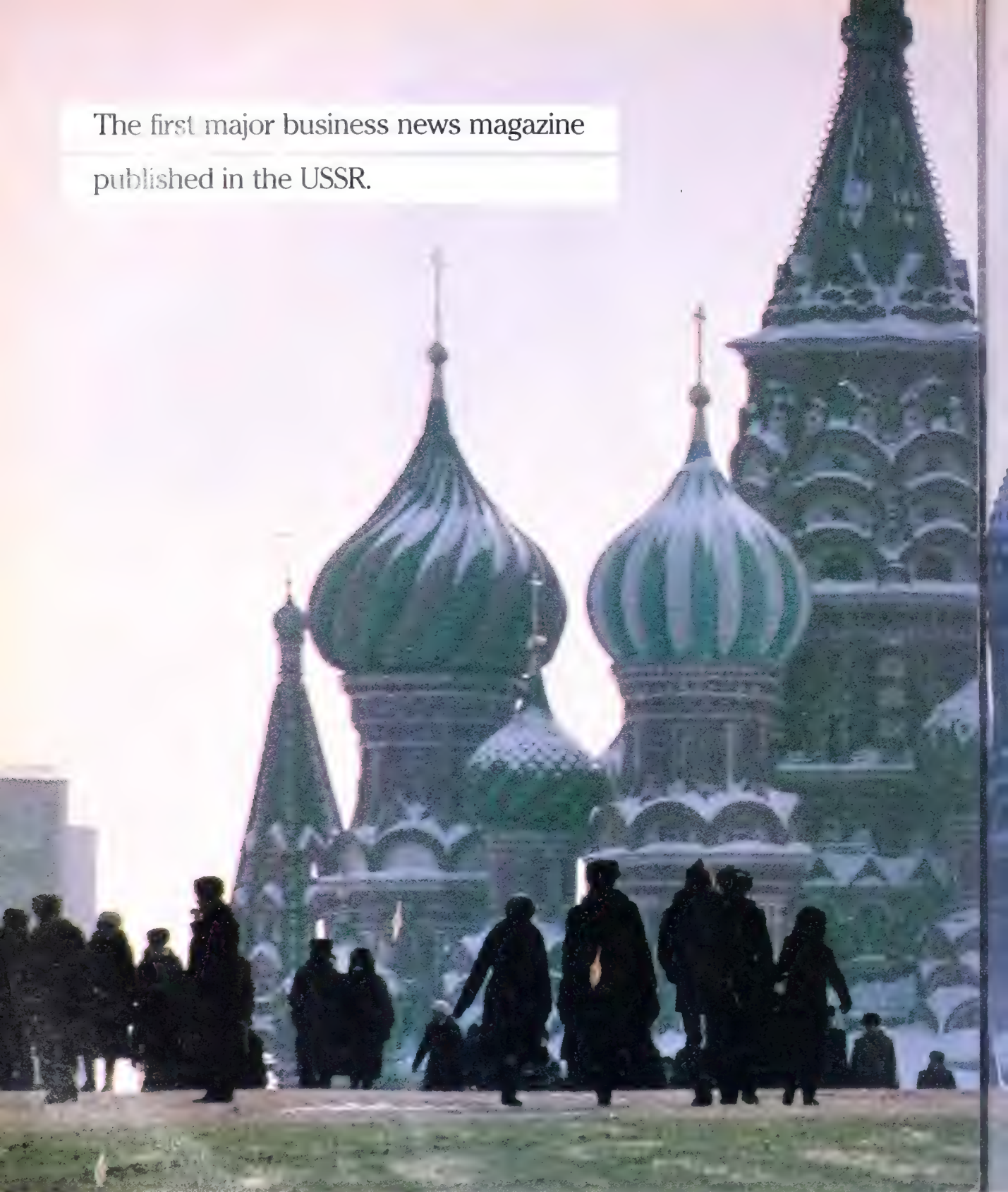
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IS ESPN IN FOR A STIFF UPPERCUT?

A merged Prime and SportsChannel would be a formidable foe

Oh, to be a sports junkie in South Florida. Turn on the Sunshine Network and you can watch the Orlando Magic pro basketball team, plus a full slate of college sports. Switch to SportsChannel Florida and you can catch the state's other NBA team, the Miami Heat. Then there's ESPN and Turner Broadcasting System, with their steady diet of pro baseball and football. And starting in 1993, either Sunshine or SportsChannel will televise games featuring Miami's new Major League Baseball team. Already, both channels are girding for a costly bidding war for TV rights.

But while viewers cheer the competition, regional cable operators around the country are calling "time out." They're worried about sinking into a crippling rivalry with other local cable channels. The nation's 32 regional sports channels would like to challenge national cable networks such as ESPN for viewers and advertising dollars. But that's tough to do if they must spend much of their money to outbid rival channels for rights to televise local baseball.

Indeed, few regional sports services are turning a profit, even though new viewers are signing up in droves (chart). "I don't worry about the broadcasters," says Dave Almstead, general manager of the Sunshine Network. "SportsChannel is the competition." So far, though, the real competition has been ESPN, which has 59 million subscribers, or 63% of homes with television. Turner's TBS and TNT networks have almost as many. **STRIKING DISTANCE.** By contrast, the largest regional sports network, Prime Network, reaches 24.8 million subscribers. Like the Big Three broadcast networks, Prime has a string of owned-and-operated channels and affiliates in major markets. Florida's Sunshine Network is one such affiliate. But while Sunshine has signed up 3 million homes in just three years, it hasn't attracted lots of national advertising. That's because

these advertisers prefer the reach and prestige of ESPN. "We don't see them competing on the national level," says Steven M. Bornstein, president of ESPN.

That may soon change. The two main regionals, Prime and SportsChannel America, have been negotiating to meld

higher ratings than the national game carried by ESPN. And the affiliates SportsChannel and Prime Network have locked up rights to virtually all local teams in their markets. ESPN televises football and baseball games, too. But with few exceptions, they aren't tailored to specific markets.

A merger would also strengthen the regionals in national programming, where ESPN now holds the edge. Prime and SportsChannel supply their affiliates with national sports to augment the local offerings. Prime delivers 50 events a year, much of it low-budget fare such as waterskiing and volleyball. Fusing the two would basically double the supply of national programming.

But the key benefit of a merger is purely financial. Because they don't collect lots of ad revenue, regional networks must rely heavily on subscriber fees. In 1990, regional networks earned \$130 million in ad revenue. But that still means subscribers must cover most of the channels' operating costs. With the escalating cost of TV rights, this translates into frequent rate hikes. A merger would make the regionals far more attractive to would-be advertisers. "It would open up a whole new pot of money," says Jonathan Mandel, a senior media buyer at Grey Advertising Inc. Also, merging local channels would dramatically reduce the costly battle for TV rights.

There are still significant hurdles. Both sides have been wrestling over the shape and management of the new organization. Prime and SportsChannel are both owned by some of the most maverick entrepreneurs in the cable business: Prime's backers include John C. Malone, CEO of Tele-Communications Inc., and cable pioneer Bill Daniels. SportsChannel is a venture of NBC Inc. and Cablevision Systems Corp., whose chairman, Charles E. Dolan, helped start Home Box Office. Between them, Malone and Dolan are responsible for much of cable's torrid growth over the past decade. If they can join forces on this playing field, cable sports may soon be more competitive than any late summer pennant race.

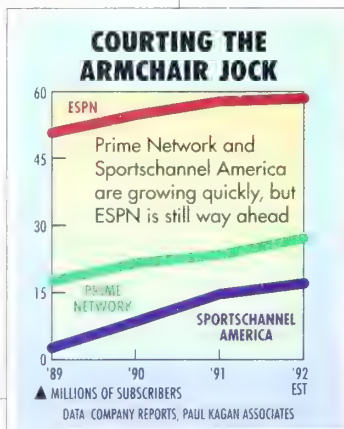
By Mark Ivey

Houston



their channels into a single network. Together, they would have 40 million subscribers. That's still fewer than ESPN. But it puts them within striking distance: "They'd be a formidable competitor for ESPN," declares Denver cable consultant Paul Bortz. The talks have proceeded in fits and starts. Nevertheless, many cable executives predict that the merger will happen by the end of the year.

That should give ESPN and the other big players pause: A new national network with strong local affiliates would have some distinct advantages. For one thing, telecasts of local teams usually win



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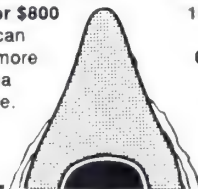
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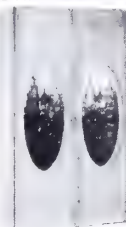
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Travel

WHEN A DREAM VACATION TURNS INTO A NIGHTMARE

Samuel and Renee Marcus had done lots of traveling, but their first trip to the Orient two years ago was unforgettable. The Long Island couple had plunked down about \$15,000 for a whirlwind, all-expense-paid tour ending in Hong Kong. But when they arrived in Tokyo, their first destination, they got word that the trip had been canceled. The tour operator, Hemphill Harris Travel, was having money problems and hadn't paid any expenses. Left stranded, they hopped on a plane home three days later.

As the Marcuses discovered, what sounds like a dream vacation when you're at the travel agency can sometimes turn into a disaster

in real life. When Hemphill collapsed, it allegedly left hundreds of vacationers with worthless travel deals. But tour operators aren't the only source of potential snags. Agents can book vacationers on flights that get canceled, and airlines can go bust.

ADVANCE TIP-OFF. Disappointed travelers are not without recourse. You can always head for court—but as a last resort. Last year, the Marcuses won the right to sue their agent, Zenith Travel, for negligence. Their suit, which Zenith is fighting, is among a growing number of cases making it easier to hold agents accountable for plans gone awry.

Ideally you want to uncover possible problems before they

mushroom. Often, all it takes is a few phone calls. Before plans are set, travelers would be wise to check with the local Better Business Bureau and the consumer-affairs division of the state attorney general. Both offices could tip you off if an airline or a tour operator is the target of frequent grumbling. For help in locating these and other information sources, the U.S. Office of Consumer Affairs publishes a free *Consumer's Resource Handbook* (Handbook, Consumer Information Center, Pueblo, Colo. 81009).

Travelers considering inexpensive charter flights and tour packages should stick to federally registered public charters. These carriers and operators must set up sepa-

rate accounts in which customers' money is held in escrow until travel is completed. The tour operators must also post a bond. The reason to go this route is simple. Says Thomas Dickerson, a traveler's lawyer in Manhattan: "Your money is protected."

Travel insurance may buy you some peace of mind. But be careful about trip-protection plans or cancellation insurance policies that are offered by tour operators. Costing from \$50 to \$100 per person, they entitle you to a refund if you cancel—if the company is still around when you come to collect.

Travel insurance from established insurance companies, however, usually goes a step further. The Travelers,

example, offers four types of protection in its Travel Ince Pak. Ranging from \$100 and up, they cover things, from lost luggage to accidents and unforeseen emergencies. The latter is especially good for folks who get stuck in traffic and miss their flights.

If you book through American Express travel agents, the Express will reimburse you for deposits or for full payments if the airline or cruise company goes bust. The U.S. Travel Operators Assn. (USTOA), a trade group, will also issue refunds if any of its 41 member stops operating or goes bankrupt. For information about members or advice on booking, write to USTOA, 10 E. 51st St., Suite 12B, New York, N.Y. 10022.

REASONABLE. If problems arise en route, try to solve them on the spot. "If the air conditioner doesn't work or if the room is dirty, don't stay more than five days," says Robert Whitley, USTOA president. He urges travelers to complain to the hotel, the tour operator, or even the travel agent back home. But be reasonable: Don't buy budget and then expect deluxe.

Travel agent gripes are legitimate, but if they'll get resolved quickly. If not, the USTOA and other trade groups may intervene on your behalf. The American Society of Travel Agents in Washington (202-739-2782) will even help file complaints.

Litigation can be costly, time-consuming, and frustrating. And it can be tough to sue a bankrupt tour operator or airlines and overbooked hotels. Partly for these reasons, the travel agent is becoming a popular target. Travel agents aren't guarantors, says Rodney Gould, Zenith's lawyer. Other experts say travelers have a right to expect accurate information about prices and traveling arrangements. But don't blame agents if events beyond their control ruin your trip.

With a little care, you can avoid vacation problems. And with a little luck, the weather will hold up. *Michele Galen*

Family

HELPING A TEEN WHO JUST CAN'T SAY NO

Few things are more heartbreaking for parents than seeing a child swept up in the drug tide. While substance abuse among teenagers is gradually declining, the government estimates that 4.9 million adolescents drink, more than a million smoke marijuana, and thousands more use stimulants or tranquilizers. As many as half of these kids may be chemically dependent.

Fortunately, treatment has grown increasingly sophisticated, with many programs tailored to teenagers. But

matches your location, income, and specific problem. A few private inpatient facilities have "scholarship beds" based on need, taking one or two patients a month for free.

Treatment can take the form of intensive detoxification and rehabilitation in a hospital or other accredited institution, usually over one to two months. Such programs average \$9,000 for a 28-day stay. The alternative is an outpatient plan involving therapy and support sessions for as long as two years. These programs usually cost \$1,000



finding the right one for your child takes research. Public programs often have waiting lists of up to six months, especially for inpatient care, and they tend to be in poor urban areas. Private facilities are very expensive, and insurers generally limit coverage for substance-abuse treatment.

HOTLINE. If your company has an employee-assistance program, find out what kind of covered treatment is available for your dependents. Or, you can call the National Institute of Drug Abuse's hotline (800 662-HELP) for a referral that

to \$2,000 a month, and some health professionals say they do a better job of reeducating an adolescent to live happily without getting high.

A responsible program will conduct a pre-admission assessment that includes tests for physical diseases, psychiatric disorders, and learning disabilities. That's because some children—just like adults—use drugs as a way of self-medicating manic depression, for example.

The evaluating team should also include trained family counselors. Kids often learn

substance abuse at home, even if parents use nothing more potent than cigarettes and beer. "Usually, one or both parents have a drug or alcohol problem," says Dr. James Cocores, medical director of outpatient recovery at Fair Oaks Hospital in Summit, N.J. In such cases, the whole family needs to learn to live without chemicals. Fair Oaks operates two adolescent outpatient programs—one with a strong educational focus for young "experimenters" and another for habitual drug users—in addition to an inpatient plan.

HEALTHY HABITS. Most programs are loosely based on the 12-step system of Alcoholics Anonymous, which stresses abstinence and strong peer support. But "it's very different from adult treatment," says Cathy Seward, head clinician at Pioneer House, a unit of Minneapolis' Hazelden clinic that specializes in 14- to 25-year-olds. Because adolescence is such an intense learning phase, kids who drink or use drugs risk a degree of developmental retardation, according to Seward. "Part of their recovery is learning how to catch up," she says. As part of this process, Pioneer House may have nutritionists or exercise trainers help kids learn healthy habits.

Straight, an unusual long-term outpatient program with 18 facilities throughout the country, separates troubled teenagers from their parents in the first phase of rehabilitation. The kids live with a family whose teenager is in a more advanced stage of recovery. Teens go home when they're ready to begin building a new life and repairing family ties. They continue outpatient therapy for up to a year, and the program also offers "aftercare" support.

Experts agree that the earlier addiction is recognized, the greater the chances of recovery. Like adults, kids who get treatment relapse at a rate of around 50%. But with each effort at sobriety, the odds improve. And ignoring addiction is like playing Russian roulette. *Joan Warner*

Health

JUST HOW STRESSFUL IS A STRESS TEST?

Taking a stress test has almost become a rite of passage for middle-aged executives. But these tests to detect coronary artery disease—the No. 1 killer in the U.S.—aren't always necessary, especially if you don't experience such telltale symptoms as chest pains or shortness of breath.

So how do you know if you need one? Adolph Hutter Jr., a cardiologist at Massachusetts General Hospital in Boston, recommends the procedure if you are over 40 and meet at least two risk factors: a family history of heart disease before age 55, a cholesterol level of at least 240, and blood pressure higher than 160/90. Smokers, diabetics, and sedentary people embarking on an exercise program are also at risk.



Once you decide to proceed, a doctor will take a resting electrocardiogram (EKG) reading to measure your heart's electrical activity. Then you climb on a treadmill. There, the doctor will attach 12 metal disks on wires from the EKG monitor to your chest. Then you walk and run on the

treadmill for about 10 minutes while the doctor monitors blood pressure, heart rate, and the EKG.

The test, designed to detect obstructed arteries, has drawbacks. The chance of its picking up significant blockage is 65%. Even if it does, it may not pinpoint location. And

there's a high rate of false positives, especially in women.

A thallium screen, for \$70 to \$1,000—about three times as expensive as the basic test—is more accurate. At the peak of exertion on the treadmill, a radioisotope that illuminates the blood enters your bloodstream through an intravenous line. Then the patient lies down, and a special camera photographs the blood flowing through the heart. The pictures do a better job of isolating areas of blockage.

WATCH YOUR DIET. Most insurers will cover either type of stress test if a patient displays symptoms. Otherwise, traditional plans often deny coverage. But managed-care programs that encourage preventive care, such as health maintenance organizations and preferred provider plans, will generally pick up the bill.

When a stress test shows blockage, it's not the end of the world. Many patients get treated with medication or, in severe cases, with bypass surgery. In one-third of cases, just exercising and watching your diet can reduce the obstruction. *Lois Therrien*

Before the surge of two-income families, the insurance industry targeted husbands. Their widows, went the pitch, would need funds for the mortgage and children's education. "But now that both partners are wage-earners, it's important to guard against the loss of either income," says Ted Lietz, at Jackson National Life in Lansing, Mich.

Instead of a husband and wife buying separate policies naming each other as beneficiary, "first-to-die" coverage may be a less costly option. One policy covers both; if either dies, the other collects.

TWO FOR ONE. The idea works best when each spouse's income is equally vital to maintain the family's lifestyle. First-to-die insurance typically saves 10% to 25% of the cost of separate policies, because premiums are based on a hypothetical "joint equal age."

Smart Money

TWO INCOMES, ONE LIFE-INSURANCE POLICY

A typical case: One insurer charges a 55-year-old husband nearly \$18,000 a year for his own \$1 million whole-life contract. A similar policy for his wife, also 55, costs roughly \$11,000. But one first-to-die policy runs about \$24,000, a 17% savings. Another insurer will sell two 35-year-olds a \$200,000 policy for \$255 monthly, vs. \$341 for separate policies.

Joint coverage isn't for everyone. An older husband might prefer to buy his own whole-life policy while his younger spouse gets low-cost term coverage.

But there are plans to suit different needs. Nationwide sells "joint decreasing term" coverage that lets a couple's surviving member pay off

any remaining mortgage sum. The "joint ultimate" policy of Jackson National and "multi-life" plan of Fidelity Union in Dallas let you build up invested funds for retirement if you surrender the policy. Life of Georgia's "joint whole life" plan "isn't only for a couple," says sales support director Carl Saunders. "It's Jim-dandy for buy-sell arrangements

where two partners own a business. If one dies, the other has the proceeds to buy his share." Some policies cover several partners with payouts pegged to each one's piece of the business.

Many also enable the survivor to do some estate planning. The policy can be converted to one that pays a matching death benefit to the heirs of the second-to-die. *Don Dunn*

THE SAVINGS IN FIRST-TO-DIE INSURANCE

ANNUAL PREMIUMS FOR \$1 MILLION OF WHOLE-LIFE INSURANCE

Separate policies Multi-life policy

For a couple . . .

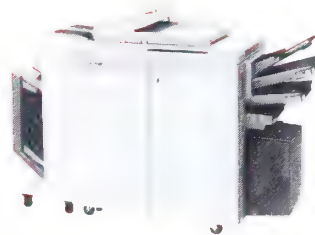
MALE, 55	\$17,974	
FEMALE, 50	11,025	
	\$28,999	\$24,151

For business partners . . .

MALE, 60	21,567	
MALE, 55	16,027	
MALE, 40	6,193	
	\$43,787	\$35,179

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Shopping

BARGAINS BY THE FORKLIFT

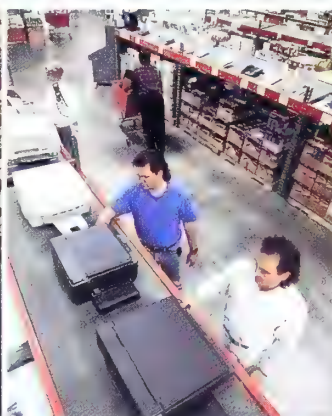
Are you in the market for a 50-pound bucket of laundry detergent? What about some 3-pound cans of tuna or a hunk of cheddar cheese about the size of a cinder block? Perhaps you'd just like to pick up a new TV, a fax machine, a set of radial tires, patio furniture, a few pairs of underwear, and 2,500 sheets of computer paper? You can find all this and more at the 400 or so warehouse club stores, with names such as Sam's, Price Club, Costco, PACE, and B.J.'s Wholesale Club, springing up across North America faster than you can say forklift.

These vast, members-only discount chains have such bargains, in fact, that they are growing faster than any other sector of the retail business. About 500 of them will be open for business in the U.S. and Canada by the end of the year. The warehouse stores—and they are, in fact, huge warehouses—sell just about everything, typically in industrial-size quantities. Most items are name-brand products, not seconds. But often it's hit or miss. If you need an air conditioner, for example, the store may carry two models—or none at all.

BULK SHOPPING. To get in the door, you have to show a card that proves you've paid your dues: usually \$25 a year. For active members, the fee is negligible in light of the in-



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credible bargains they can find. Goods are marked up 8% to 10% vs. the typical 20% to 30% markup in a regular discount store or 35% to 50% in a department store. At Costco, a \$600 Ralph Lauren suit sells for \$269.99, and two 32-ounce bottles of Scope mouthwash, regularly \$9.78, go for \$6.99.

Many customers here aren't your typical shopping-cart set. About one-third are business owners, using the warehouse membership to buy goods in bulk for their restaurants, gas stations, grocery stores, or small offices. They account for more than 60% of sales.

Most stores set aside exclusive hours for them to shop.

Individuals used to be able to get a membership at no cost, but they had to pay a 5% surcharge on the posted prices. In some places, especially the Midwest, that's still true. But most of the warehouses are switching to all paid memberships and eliminating the surcharge.

Still, most chains won't accept just anybody: You have to prove you belong to a certain credit union or work for the government or an approved school, hospital, or company. A few chains are doing away with these restric-

tions, but others find them useful: Customers affiliated with such organizations as wage earners and less likely to write bad checks. With the proper credentials, you can sign up, pay your fee at the door, and start shopping.

NO DELIVERIES. Don't confuse warehouse stores with a trip to the local mall: There's little sales assistance, no decor, no deliveries, no frills. Nobody will help you load bulky purchases into your car. Goods are stacked up high, and you may have to dodge forklifts. At the cashier, one person shouts out a number for each item while the other punches the register. Only cash and checks are accepted.

If you have a choice of warehouses, you won't find much difference. Prices and merchandise are much the same—though one store may have an edge over another in a particular type of merchandise. Innovations, such as fresh bakery items, optical departments, pharmacies, film processing, and car price prenegotiated with nearby dealers, are quickly copied by other warehouses.

With 3,500 items per store, warehouses don't have large selections in each merchandise category. You still need supermarkets and office-supply stores for special needs. And the clothing selection will never put department stores out of business. But the warehouse formula works. For those who think they're going just to stock up on toilet paper and soap, watch out. You may come home with a capucino maker and a six-foot houseplant. *Dori Jones Yan*

Worth Noting

■ **GIFTED GUIDE.** *Nurturing the Gifted Child*, American Mensa's resource guide for parents, lists associations, selected readings, and university-based summer programs for gifted children. For a free copy, call 718 934-3700.

■ **PLASTIC PERK.** The latest credit-card enhancement: "Lemon Assurance" from American Express. If you pay for a warrantied item with any AmEx card, including Optima, the service will replace the item—excluding cars—the second time it breaks down. The first time, it must be repaired under

warranty. For details, call 800 322-7410.

■ **WILD GAME.** Play golf and see giraffes at the same time on African Wildlife & Travel's 13-day golf safaris in Zimbabwe. The \$1,800 land package includes greens fees and visits to Hwange National Park and Victoria Falls. Call 212 308-2607.

Index to Companies

Index gives the starting page for a story or feature with a significant reference to a company. Most companies are indexed under their own names. Companies listed only in tables are not included.

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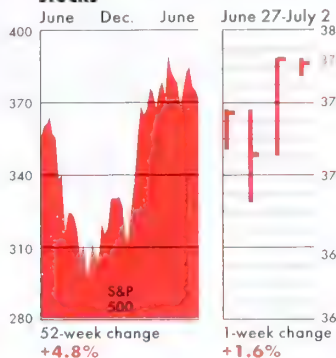
The right choice

Investment Figures of the Week

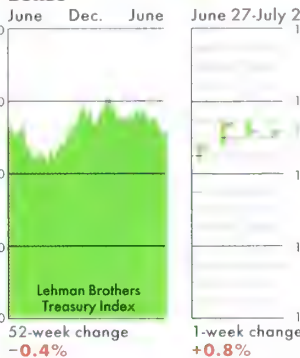
COMMENTARY

Stock market recovered some ground that it had lost in previous weeks. The Dow Jones industrial average gained nearly 100 points on July 1, as investors were buoyed by a rally in Tokyo and by cheerful economic data. Purchasing managers' index signaled a revival in manufacturing. But the market petered out the following day, as broad market indicators ebbed, even though the Dow rose—spurred by gains in Disney stock.

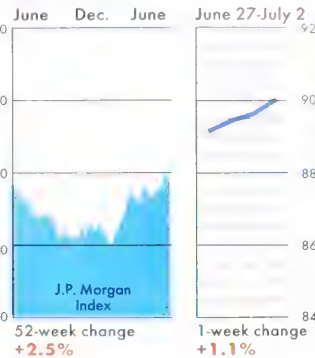
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS

	Latest	% change Week	% change 52-week
DOW JONES INDUSTRIALS	2972.7	2.0	2.1
SMALL COMPANIES (Russell 1000)	196.9	1.7	5.2
TECHNICAL COMPANIES (Russell 2000)	168.2	0.4	-0.4
INDUSTRIAL COMPANIES (Russell 3000)	209.1	1.6	4.8

FOREIGN STOCKS

	Latest	% change (local currency) Week	% change (local currency) 52-week
LONDON (FINANCIAL TIMES 100)	2460.2	0.7	3.7
TOYO (NIKKEI INDEX)	23,995.8	1.0	-26.0
TOKYO (TSE COMPOSITE)	3493.6	0.4	-1.9

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.7%	5.7%	8.0%
30-YEAR TREASURY BOND YIELD	8.4%	8.5%	8.4%
S&P 500 DIVIDEND YIELD	3.4%	3.3%	2.9%
S&P 500 PRICE/EARNINGS RATIO	18.0	17.7	16.6

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 26-week moving average	366.2	364.8	Positive
Stocks above 26-week moving average	59.8%	59.5%	Neutral
Speculative sentiment: Put/call ratio	0.52	0.58	Positive
Insider sentiment: Vickers sell/buy ratio	2.73	2.33	Negative

INDUSTRY GROUPS

4-WEEK LEADERS

	4-week	52-week
GOLD MINING	10.6	-9.6
AFTERMARKET AUTO PARTS	10.3	13.0
METAL AND GLASS CONTAINERS	5.7	19.8
HARDWARE AND TOOLS	3.6	0.0
DRUG CHAINS	3.1	28.8

4-WEEK LAGGARDS

	4-week	52-week
HOTELS AND MOTELS	-13.4	-24.2
NATURAL GAS DISTRIBUTION	-13.1	-21.6
OIL WELL EQUIPMENT AND SERVICES	-13.0	-10.0
PUBLISHING	-12.2	-3.3
SEMICONDUCTORS	-12.2	-11.0

Strongest stock in group

	4-week	52-week	Price
ECHO BAY MINES	19.7	-23.3	9 7/8
GOODYEAR TIRE & RUBBER	28.6	12.0	33 3/4
BALL	6.7	2.4	31 7/8
BLACK & DECKER	4.9	1.6	16
WALGREEN	5.0	37.2	34 1/8

Weakest stock in group

	4-week	52-week	Price
MARRIOTT	-20.0	-20.9	18
COLUMBIA GAS SYSTEM	-52.6	-57.1	19
McDERMOTT INTERNATIONAL	-31.1	-39.2	18 1/4
TIME WARNER	-26.7	-12.1	88 3/8
INTEL	-18.4	-3.2	45 1/2

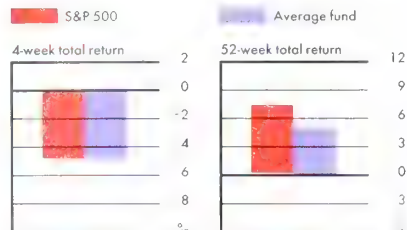
BRIDGE INFORMATION SYSTEMS INC

MUTUAL FUNDS

LEADERS

	4-week total return	%		4-week total return	%
STRATEGIC INVESTMENTS	12.9		EQUITY STRATEGIES	-14.3	
FINANCIAL STRATEGIC GOLD	8.1		FIDELITY SELECT COMPUTERS	-13.6	
BENHAM GOLD EQUITIES INDEX	7.9		FIDELITY SELECT ENERGY SERVICE	-13.1	
	52-week total return	%		52-week total return	%
FIDELITY SELECT BIOTECHNOLOGY	49.7		BULL & BEAR SPECIAL EQUITIES	-43.5	
FIDELITY SELECT HEALTH CARE	44.9		STEADMAN OCEANOGRAPHIC TECHNOLOGY	-40.3	
FIDELITY SELECT MEDICAL DELIVERY	43.3		UNITED SERVICES EUROPEAN EQUITY	-33.2	

MORNINGSTAR INC



RELATIVE PORTFOLIOS

Dollar amounts represent the present value of \$10,000 invested one year ago in each portfolio.

Percentages indicate 1-day total returns.

Treasury bonds
\$10,814
0.00%

Money market fund
\$10,615
+0.11%

U. S. stocks
\$10,563
-0.93%

Gold
\$10,436
-1.78%

Foreign stocks
\$10,388
+0.08%

DATA RESOURCES INC

Data on this page are as of market close Tuesday, July 2, 1991, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of market close July 1.

Mutual fund returns are of June 28. Relative portfolios are valued as of July 1. A more detailed explanation of this page is available on request.

BANKING REFORM: JUST A MINUTE, PLEASE

The Administration's proposal for banking reform is making far more headway than most experts thought it would six months ago. The sweeping measure easily passed the House Banking Committee on June 28, though it still faces skeptical scrutiny from House Energy & Commerce Committee Chairman John D. Dingell (D-Mich.).

And well it should. Virtually everyone agrees that banks ought to be allowed to have branches in more than one state, both to diversify their risks and to achieve cost savings through consolidation and the shedding of excess capacity. But other aspects of the overhaul are more debatable.

The Banking Committee bill shirks the necessity for new, stricter limits on deposit insurance. In particular, the failure to curb insurance coverage of brokered deposits is inexcusable. Wealthier customers and securities firms that bundle deposits together to reap higher rates must be convinced that larger rewards entail larger risks—including the palpable risk that taxpayers will not automatically cover their losses. Congress must recognize that mandating stricter regulation, as the House bill does, is a poor substitute for limits on deposit insurance (page 122).

Allowing banks to sell insurance and underwrite securities seems unobjectionable in principle. These new activities are supposed to operate separately and be separately capitalized with funds that are not drawn from insured deposits. The key is devising a fire wall that guarantees to the taxpaying public that it will not have to empty its pockets if these new lines of business don't pan out. Allowing giant industrial corporations to purchase banks, however, raises the thorny issue of ensuring that such conglomerates are not tempted to discriminate against competitors in their lending activities. We oppose extending the industrial ownership of banks.

A decade ago, Congress created a time bomb by unleashing thrifts to make money in new kinds of ways. The argument that banks are different flies in the face of the 1,000-plus bank failures of the last five years, the parlous current financial condition of many large banks, and the prospect of yet another taxpayer-financed rescue. Lawmakers should weigh their reform proposals carefully to ensure that this time they don't make matters worse.

THE REAL STRENGTHS OF EMPLOYEE OWNERSHIP

Don't write an obituary for employee stock-ownership plans just yet. Although Congress last year did away with many of the tax incentives that originally sparked corporate interest in ESOPs, they are proving to be more popular than many people imagined (page 108). A new study indicates that the total worth of worker-owned stock in public corporations probably exceeds \$150 billion, including an average of 12% of the shares of some 1,000 large,

publicly held companies that employ 11 million workers.

The appeal of ownership programs goes far beyond the tax breaks available to ESOPs. At a time when competitive pressures are forcing companies to keep a lid on labor costs, many are using stock plans as a substitute for cash compensation. Stock is being used to fund bonuses, pension and savings plans, and even retiree medical benefits.

Such programs are not without risk, particularly if corporate sponsors go belly-up in future years. But they can help make companies more competitive, enhance productivity and bolster morale when wage hikes need to be deferred. Because workers are concerned with job security, they represent a source of patient capital that is likely to value long-term performance over short-term profits.

The most intriguing aspect of this trend is the possibility that workers who own a significant share of their companies will want a voice in corporate governance, as has already happened in the case of several companies contemplating mergers. Employers who prepare for this development by setting up mechanisms for dialogue can lay the groundwork for productive cooperation between labor and management in future decision-making. Those who don't may find worker ownership a mixed blessing.

BUSINESS SHOULD RALLY ROUND THE LABS

The economic recession may be ending, but not the recession in corporate spending for research and development. A recent survey by this magazine (BW—July 1) indicates that R&D outlays by U.S. companies rose just 2.2% last year in inflation-adjusted terms—the second smallest increase in 15 years. And the National Science Foundation projects no real growth at all in such spending this year.

The fact that the R&D slump reflects both the sluggish economy and government cutbacks in defense does not lessen its dire implications for U.S. competitiveness. Other nations facing slowdowns have managed to keep such investment on a rising course—from 2.8% to 7.5% in real terms in Canada, Germany, Italy, and France last year. What's more, there are signs that U.S. companies are neglecting their strongest suit: basic research aimed at new technologies and products. Stung by Japan's prowess in applying the fruits of research to quality product development, they are finally concentrating on upgrading their product lines. Unfortunately, many also appear to be cutting back the kind of high-risk research that leads to new products and technologies.

Clearly, R&D investment cannot be hostage to the vagaries of the market and the business cycle if the U.S. is to maintain its competitive vitality. The government, which sponsors roughly half of the nation's R&D, needs to lead the way—by shifting more of its focus from such areas as defense and aerospace to emergent civilian technologies and by making the R&D tax credit permanent. And Wall Street needs to find a better way of valuing research efforts. In the end, however, it is companies that must resist short-term pressures and recognize that balanced and sustained R&D is essential to their growth and survival.

July 22

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SYNERGY?

Not much.

STRATEGIC ALLIANCES?

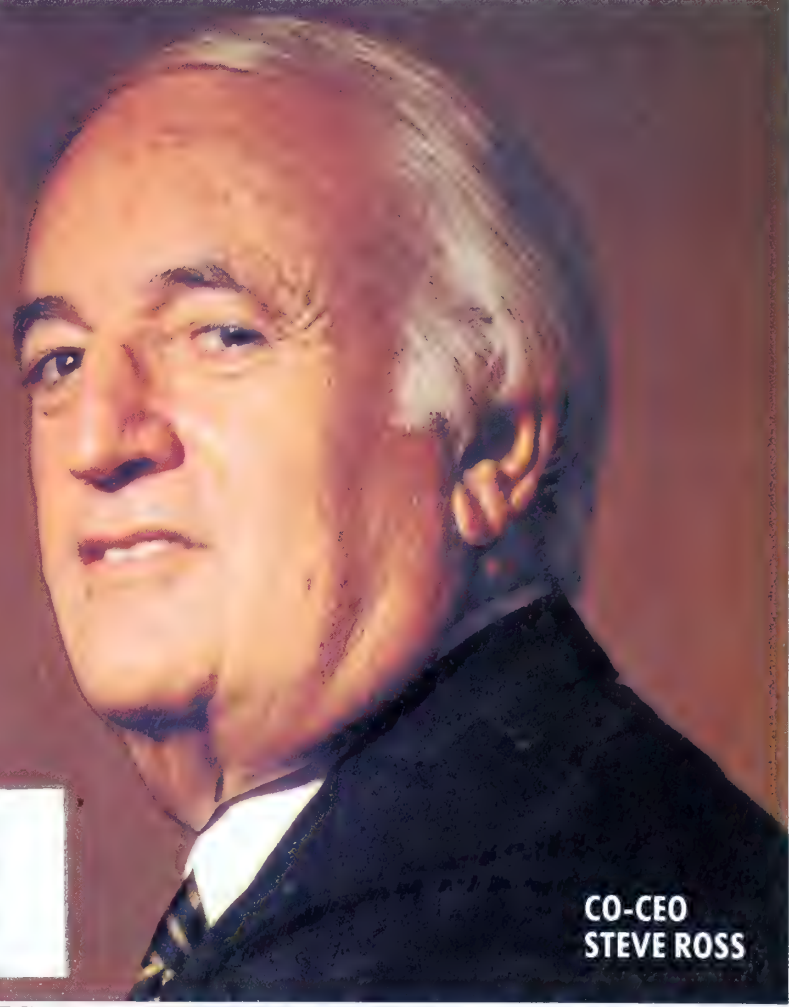
Not yet.

RIGHTS OFFERING?

Not so fast.

No wonder
shareholders
are mad.

PAGE 70



CO-CEO
STEVE ROSS

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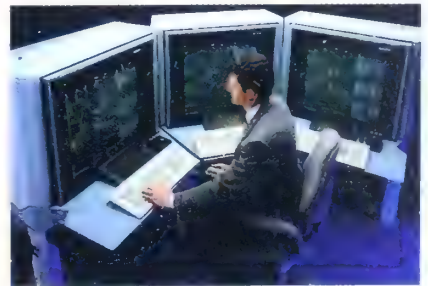
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HUGHES

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BULL'S EYE: WARNER WILL MAKE A TIDY PROFIT DISTRIBUTING *ROBIN HOOD*—THOUGH THE LION'S SHARE GOES TO THE PRODUCERS

Cover Story

70 TIME WARNER

Steve Ross made \$78 million last year, and now he has the headaches to match. A \$4.3 billion loan is coming due, and it will be a stretch. Not that Time Warner is broke: Its cash flow is more than \$2 billion a year. But the big benefits that Ross promised would come from the merger simply haven't materialized—suggesting that his rationale for fusing the two giants may have been fundamentally flawed

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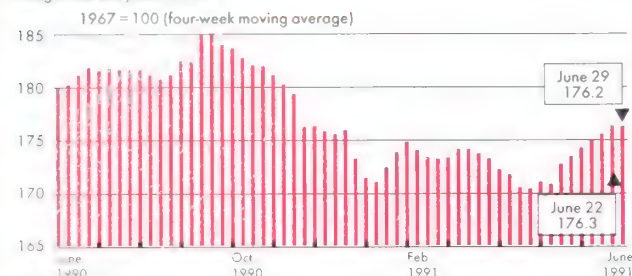
Greenspan's new challenge How to prevent future BCCIs It's time to reward South Africa

BusinessWeek Index

PRODUCTION

Change from last week: 0.1%

Change from last year: 3.1%



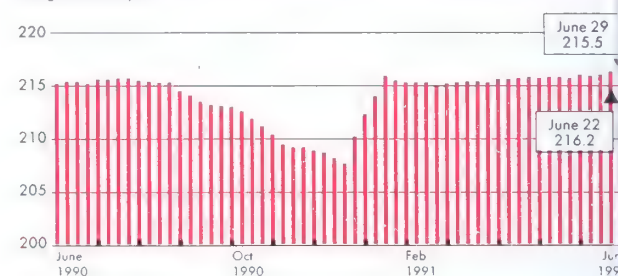
The production index was little changed for the week ended June 29. On a seasonally adjusted basis, output of lumber, trucks, coal, and rail-freight traffic fell sharply, and crude-oil refining, paper, and paperboard production declined as well. Steel, auto, and electric-power output increased. Prior to calculation of the four-week moving average, the index dropped to 174.9, from 177.8. For all of June, the index rose to 176.2, from 173.8 in May.

BW production index copyright 1991 by McGraw-Hill Inc

LEADING

Change from last week: -0.3%

Change from last year: 0.2%



The leading index was down for the week ended June 29, as no indicator gave a positive signal. Lower stock prices, faster declines in materials prices, a large increase in the number of business failures, and slower growth rates for real estate loans and M2 all contributed to the decline. Bond yields were unchanged. Before calculation of the four-week moving average, the index fell sharply to 213.9, from 216.7. For the month of June, the index dropped to 215.5, from 215.8 in May.

Leading index copyright 1991 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (7/6) thous. of net tons	1,573	1,593#	-12.2
AUTOS (7/6) units	55,567	125,695r#	-17.9
TRUCKS (7/6) units	37,078	78,010r#	1.2
ELECTRIC POWER (7/6) millions of kilowatt-hours	63,304	62,984#	1.7
CRUDE-OIL REFINING (7/6) thous. of bbl./day	13,645	13,906#	-3.8
COAL (6/29) thous. of net tons	17,004#	19,481	-2.2
PAPERBOARD (6/29) thous. of tons	763.7	748.4r	-4.0
PAPER (6/29) thous. of tons	736	756.0r	0.5
LUMBER (6/29) millions of ft.	513.0#	548.1	9.6
RAIL FREIGHT (6/29) billions of ton-miles	18.6#	19.7	-5.1

Sources: American Iron & Steel Inst., Ward's Automotive Reports, Edison Electric Inst., American Petroleum Inst., Energy Dept., American Paper Inst., WWP, SFPA, Association of American Railroads

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (7/5) S&P 500	374.70	371.75	4.0
CORPORATE BOND YIELD, Aaa (7/5)	9.04%	9.04%	-2.0
INDUSTRIAL MATERIALS PRICES (7/5)	98.7	98.8	-2.0
BUSINESS FAILURES (6/28)	399	368	46.0
REAL ESTATE LOANS (6/26) billions	\$403.9	\$405.6	7.0
MONEY SUPPLY, M2 (6/24) billions	\$3,399.5	\$3,403.9r	3.0
INITIAL CLAIMS, UNEMPLOYMENT (6/22) thous	423	431	15.0

Sources: Standard & Poors, Moodys, Journal of Commerce (index: 1980=100), Dun & Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. CIBCR seasonally adjusts data on business failures and real estate loans

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
BUSINESS WEEK PRODUCTION INDEX (June)	176.2	173.8r	-3.0
BUSINESS WEEK LEADING INDEX (June)	215.5	215.9r	0.0
EMPLOYMENT, CIVILIAN (June) millions	116.9	116.6	-1.0
UNEMPLOYMENT RATE, CIVILIAN (June)	7.0%	6.9%	32.0

Sources: BW, CIBCR, BLS

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (6/24)	\$858.6	\$860.5r	6.0
BANKS' BUSINESS LOANS (6/26)	309.0	309.9	-4.0
FREE RESERVES (6/26)	989	451r	55.0
NONFINANCIAL COMMERCIAL PAPER (6/26)	148.9	151.2	0.0

Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed for two-week period in millions)

MONEY MARKET RATES

	Latest week	Week ago	Year ago
FEDERAL FUNDS (7/9)	5.82%	6.38%	8.28%
PRIME (7/10)	8.50	8.50	10.00
COMMERCIAL PAPER 3-MONTH (7/9)	6.14	6.11	8.13
CERTIFICATES OF DEPOSIT 3-MONTH (7/10)	6.04	6.04	8.25
EURODOLLAR 3-MONTH (7/6)	6.06	6.08	8.19

Sources: Federal Reserve Board, First Boston

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (7/9)	139	139	148
GERMAN MARK (7/9)	1.82	1.83	1.65
BRITISH POUND (7/9)	1.62	1.60	1.80
FRENCH FRANC (7/9)	6.15	6.21	5.53
CANADIAN DOLLAR (7/9)	1.15	1.14	1.16
SWISS FRANC (7/9)	1.57	1.58	1.40
MEXICAN PESO (7/9)	3,012	3,008	2,867

Sources: Major New York banks. Currencies expressed in units per U. S. dollar, except for British pound expressed in dollars.

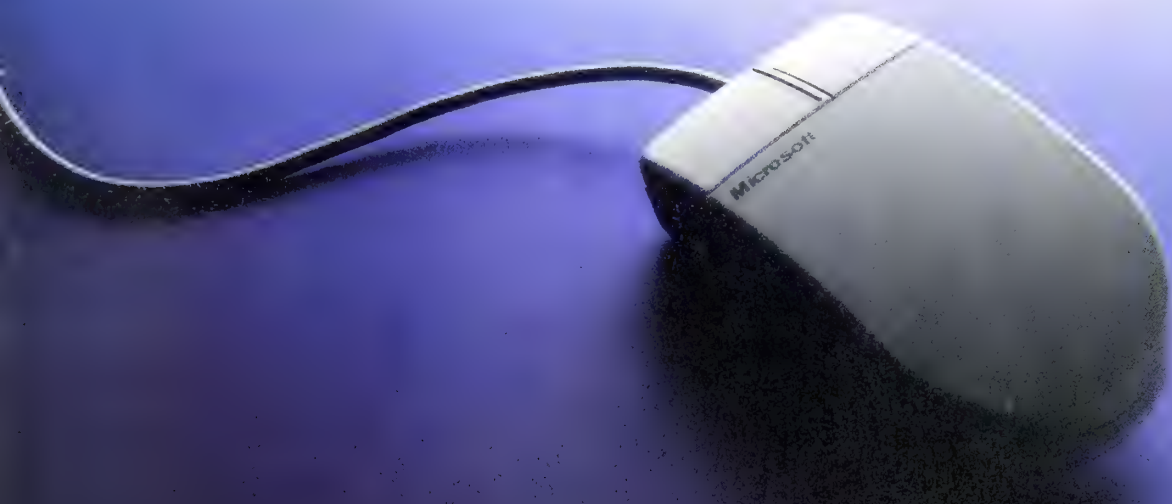
PRICES

	Latest week	Week ago	% Change year ago
GOLD (7/9) \$/troy oz.	370.900	367.100	4.7
STEEL SCRAP (7/8) #1 heavy, \$/ton	89.00	89.00	-19.5
FOODSTUFFS (7/7) index, 1967=100	194.9	196.2	-14.1
COPPER (7/6) c/lb.	106.3	105.0	-11.6
ALUMINUM (7/6) c/lb.	60.5	59.8	-16.6
WHEAT (7/6) #2 hard, \$/bu.	2.88	2.93	-11.4
COTTON (7/6) strict low middling 1-1/16 in., c/lb.	73.95	77.55	-7.0

Sources: London Wed. final setting, Chicago mkt., Commodity Research Bureau, Metals Week, Kansas City mkt., Memphis mkt.

#Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment
1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

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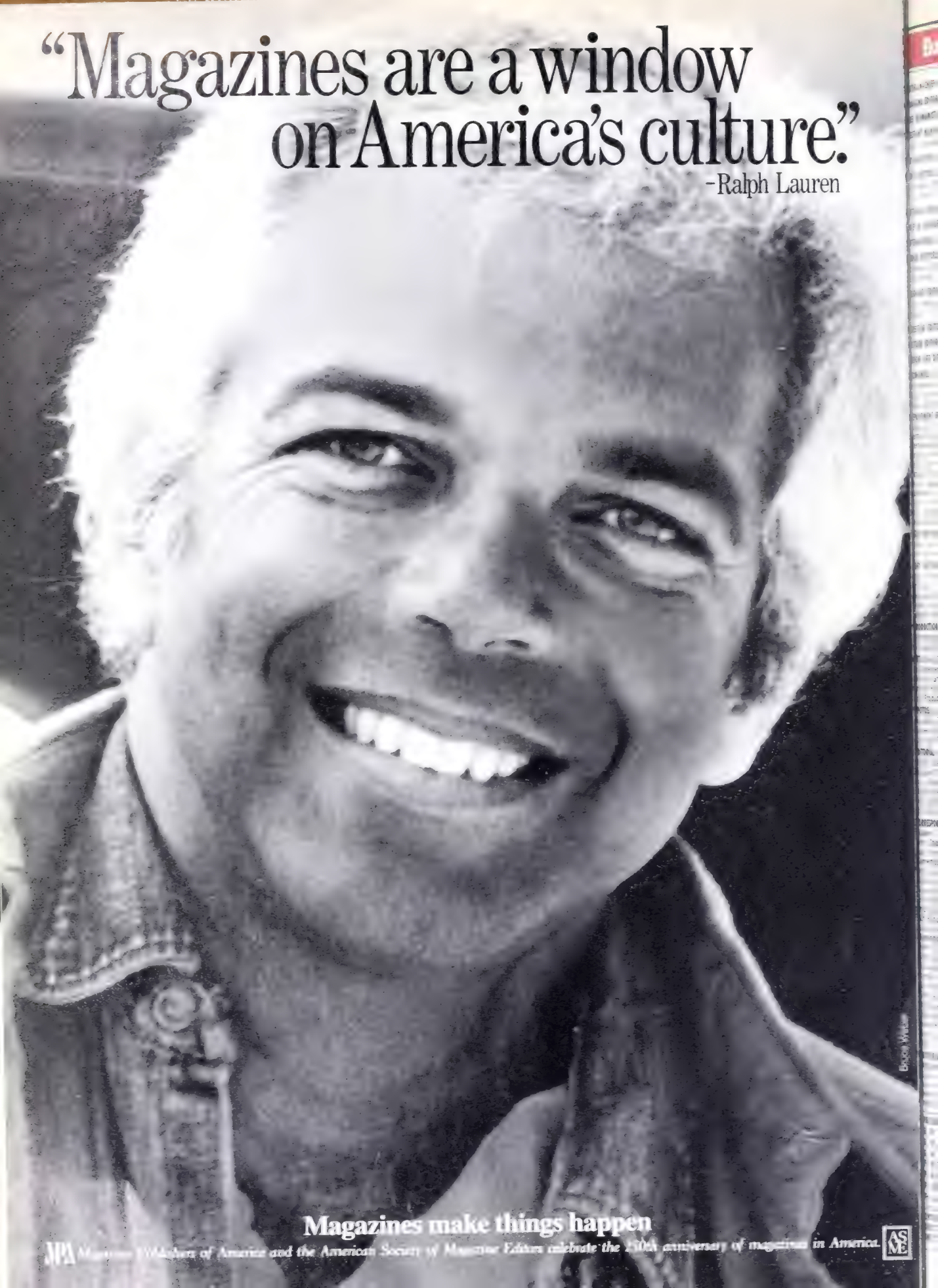
From Los Angeles Int'l	10 Flights	From San Francisco	8 Flights
From Orange County	4 Flights	From Oakland	5 Flights
From Burbank	3 Flights	From San Jose	5 Flights
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Readers Report

savings rate would have been significantly lower in the early '80s had IRAs not existed. It is ironic that while you question the ability of tax policy to promote saving, you have no difficulty accepting that it did encourage debt.

Although current estimates put the projected revenue loss for Super-IRAs at \$25 billion over five years, I do not understand why you consider this "betting the ranch." The projections are static and assume no incremental effect of new savings on the economy. Increases in savings reduce the cost of capital, encourage investment in business and infrastructure, and increase productivity and real wages, thereby expanding the economy and government revenue.

John L. Steffens
Executive Vice-President
Merrill Lynch & Co.
Plainsboro, N.J.

When your writers express bewilderment at our low savings rate, I pause to wonder if they underestimate the intelligence of the public.

Why save cash (and its equivalent) when taxes and inflation exceed the interest? Why save through real estate or security investments when taxes on interest, dividends, and capital gains make the risk-reward ratio unfavorable? We even have to pay a confiscatory capital-gains tax on the inflation-enhanced sale proceeds of a residence!

Our savings rate would improve if Congress could alter our tax law's long-time bias favoring borrowers and could reduce deficit spending.

K. Stanley Thompson
Pebble Beach, Calif.

HE WON'T LEAVE HOME WITHOUT IT

I prefer using American Express to the bank cards I hold, because of the company's unequivocal dedication to its cardholders' interests ("AmEx fights to discourage defectors," *Finance*, July 1). This point was driven home to me when I recently had to challenge an incorrect charge on a bank-issued card. I spent nearly 20 minutes negotiating through a voice-mail system, explaining the problem, arguing over interest charges, and convincing the representative of the validity of my claim. Since my experience with that bank-card-only merchant, any establishment's refusal to honor my American Express card sets off a red flag. Such companies as U-Haul, Carnival Cruise Lines, and Joan Cook are welcome to keep those extra cents. I'll take my business elsewhere.

Kevin G. Barkes
Library, Pa.

ONE OF THE BEST OF '91 LOOKS EVEN BETTER

We were pleased to be included in your story "The best of 1991 so far" (*Midyear Investment Outlook*, June 24), but I fear there was an error in the description of the fund we manage. The article states: "Using futures and options, Deo seeks to match at least 90% of the rise in the Standard & Poor's 500-stock index and absorb no more than 90% of the S&P's losses." It should read instead: "... absorb no more than a 10% loss in the fund." There is rather a large difference.

Ravindra Deo
Vice-President
Leland O'Brien Rubinstein Associates
Los Angeles

WHY GO-VIDEO'S DOUBLE-DECKER IS WORTH THE EXTRA BREAD

In reference to a quotation that was attributed to me in "The double-deck woes of Go-Video" (*The Corporation*, July 1), I did say that much of the effect of the VCR-2 could be accomplished by hooking two VCRs together with cable. But at the same time, I said that the VCR-2 was a unique product and that it saved the effort and complexity of making that kind of jerry-built hookup. You quoted part of my statement, which actually was to the effect that VCR-2 was basically more than a box with two VCRs in it because of the switching and other special circuitry.

I did express my belief that VCR-2 was a niche market product that had a special appeal. In addition, I forecast that success would bring out a number of imitations.

David Lachenbruch
Editorial Director
Television Digest
New York

ARE DIEHARD TOYOTA OWNERS KILLING DETROIT?

In reference to "The Japanese borrow Detroit's favorite ploy: Rebates" (*Top of the News*, June 17): If the DeLaHayes are accurate representatives of a larger trend, then I must say that I have greatly diminished respect for baby boomers as a group.

It doesn't seem to matter that Detroit is now building some very good cars. Import buyers seemingly will use any excuse to justify their prejudices. They are sending jobs and money out of this country with every import they purchase and compromising our children's future in the process.

If Detroit suffers too greatly, the U.S. as a whole will suffer as well.

William A. Wilfon
Chicago

It burns me up to see an American family proud to stand beside their Japanese car. Ask the DeLaHayes if they know why half the states in this country are in severe financial difficulty, why California has a \$12 billion deficit, why New York has to cut back on education, why our standard of living is declining, why nobody can find a job, and why Japan is buying up the United States.

Tell the DeLaHayes we have them to thank for the above, and when they are out of a job and hungry they can eat their Toyota.

Michael Weiner
Chestnut Ridge, N.Y.

WHERE THOSE VIRUS NUMBERS REALLY CAME FROM

The recent item on computer viruses ("Have computer viruses turned into a plague?" *Developments to Watch*, June 10) spotlighted the growing threat of infection produced by these dangerous programs.

However, the risk projections cited stem from a study by Certus Inc., not by the Data Processing Management Assn. (DPMA). The cited figures, together with contrasting views, were presented at a national computer virus and security conference sponsored by DPMA's Financial Industries Chapter. Details are reprinted in the conference proceedings.

Richard G. Lefkowitz
President
DPMA Financial Industries Chapter
New York

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The breweries and the alcohol-abuse action groups can try to place the blame hither and yon, but nothing will begin to change until we get beer ads off of our most accessible medium, TV ("It isn't Miller time yet, and this Bud's not for you," *Top of the News*, June 24). Cigarette and liquor commercials are gone; now it's time to get beer off the air. Relegate it to the printed form only. Heaven forbid a teenager should pick up a periodical and be "influenced."

Thomas R. B. Stewart
Fairfax, Va.

Letters to the Editor should be sent to Reader Report, Business Week, 1221 Avenue of the Americas, New York, N.Y. 10020. Fax: (212) 512-4464. Telex: 12-7960, Intl. 4998204. All letters must include an address and daytime and evening telephone numbers. We reserve the right to edit letters for clarity and space.

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WHAT GOES UP: THE GLOBAL ASSAULT ON OUR ATMOSPHERE

By John J. Nance

Morrow • 324pp • \$20

IS THE SKY REALLY FALLING?

James Hanson, director of NASA's Goddard Institute for Space Studies, faced a Senate hearing in June, 1988, to address a burning issue: Was the climate getting warmer as a result of the greenhouse effect? Hanson sprinkled his response with caveats and said that the summer's heat wave and drought couldn't be blamed on global warming. But he did say that "the greenhouse effect has been detected, and it is changing our climate now." Those remarks wound up in headlines proclaiming that the drought was a product of global warming. They unleashed a storm of disagreement among Hanson's peers. And the dispute over whether the planet is warming still rages.

In *What Goes Up: The Global Assault on Our Atmosphere*, John J. Nance helps put the controversial issues of global warming and the damage to the ozone layer in perspective. He begins by describing the 15 years of wrangling that finally led scientists, politicians, and business to agree that chlorofluorocarbons (CFCs) were destroying the earth's protective ozone layer and to the landmark Montreal Protocol, which phases out the chemicals. He also fleshes out what is and is not understood about global warming. While providing a fascinating glimpse of scientists and the scientific process at work, Nance also shows how slow the route can be from the first scientific identification of a serious problem to public policy that attempts to address the issue.

Nance explores ozone loss through the experiences of the scientists who pieced together the evidence that CFCs were the culprits. His vivid, you-are-there narrative drives home how fraught with disagreements and errors the process was.

The ozone wars, as Nance calls them, began in 1974, when two University of California at Irvine chemists, Sherwood "Sherry" Rowland and Mario Molina, published a theory to explain what happens to CFCs after they are released. It

was a bombshell. CFCs, they said, wend their way slowly into the stratosphere and decompose, releasing chlorine atoms. These atoms break down ozone, and that would lead to a gradual decrease in the ozone layer that protects earth from radiation. The chemists could offer no evidence of ozone loss, however, nor of elevated levels of chlorine in the atmosphere. The theory was promptly denounced by the chemical industry and disputed by other scientists.

Support didn't come until 1985, when Joe Farman of the British Antarctic Sur-

ozone. At every point, environmentalists and industry clashed over the validity of the findings. The chemical industry continually demanded more proof. The disagreement kept Washington paralyzed.

Nance considers the current debate over whether a global warming has begun and what effect it might have on climate to be at the same point the ozone issue was in 1975. Findings indicate a warming may have begun, but very much in dispute among scientists, industry, and government. With both issues, as Nance points out, the key question has been: When does society have enough proof to justify action? A global warming that means curbing carbon dioxide emissions.

As those in the "act now" camp see it, industry and other entrenched interests oppose corrective action because it would interfere with profits. But industry is legitimately opposed to environmental laws that require huge investments unless they are absolutely necessary. It boils down to assumptions: Should you assume that what you don't know can't hurt? Or should you act on the assumption that it can?

In Nance's view, the ozone wars dramatize the perils of failing to embrace the latter assumption. The discovery of the ozone hole proved that atmospheric change is not necessarily linear. Any climate change kicked off by global warming could be sudden, exponential, and unpredictable.

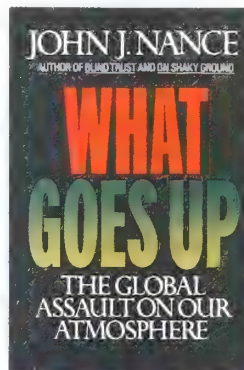
Nance is clearly impatient for action on global warming. He considers the consequences of warming risky enough to justify action now, even though scientists don't agree that warming has begun. He blames at least some of the foot-dragging on scientists' failure to communicate the issues clearly. In addition, he thinks the media's tendency to reduce complex issues to sided conflicts exaggerates the disagreement among scientists, creating an obstacle to public understanding.

To those familiar with the politics of public policy, Nance's analysis of the stumbling blocks to change will come as no surprise. His major prescription—better communication—is ill-defined, but for those who wonder what the hold-over global warming is all about, Nance's lucid explanations of this complex issue make the book worthwhile.

BY EMILY T. SMITH

Smith is Science editor of *BUSINESS WEEK*.

Nance helps put the issues of global warming and the ozone layer in perspective



vey published the first data that showed a hole was appearing in the ozone layer each winter over Antarctica. What Farman documented was not the linear decline Rowland and Molina predicted, but an exponential loss of 40% during the 1984 winter, far greater than the first small decline he detected in 1981.

Farman's paper stunned the scientific community. Other groups monitoring the atmosphere in Antarctica hadn't reported any decrease. Scientists at NASA's Goddard Space Flight Center quickly reviewed their own data and made a chilling discovery: Their instruments had recorded the losses, but the computer interpreting the results had been programmed to ignore readings that deviated so far from normal.

Nance goes on to describe how scientists verified the findings, discovered losses over the Arctic, and determined the process by which chlorine destroys

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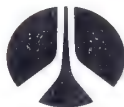
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TIME IS NOT ON AMERICA'S SIDE

BY ALAN S. BLINDER



Want to feel better about how 'lazy' Americans stack up against the 'superefficient' Japanese? Look at how similarly they allocate their time. But if you want to get depressed, look at how U.S. and Japanese children spend their days

Most of us turn time into money regularly. While the rate of exchange—our wage rate—may not be all we would like, making this swap is no great feat. Turning money into time is much harder. There are, of course, ways to perform the 20th century version of alchemy—you can hire a gardener and a housekeeper, for example. But, in general, we have only limited opportunities to buy time with money.

In that sense, the ultimate scarce resource for many people is not money but time. How people spend their time may reveal more about a society than how they spend their money. Unfortunately, while mountains of statistics and volumes of research testify to how people use their money, we have only fragmentary evidence on how they use their time. That's why a research paper by F. Thomas Juster and Frank P. Stafford, just published in *The Journal of Economic Literature* and excerpted in the Conference Board's *Economic Times*, is so fascinating.

The two University of Michigan economists review survey data on time usage accumulated over two decades and cover a variety of countries. The data come from time diaries, which, while far from perfect, provide the most accurate measurements we have. In this short space, I will focus on recent comparisons between Americans and the allegedly superefficient and highly motivated Japanese. In general, the statistics do not suggest that Americans are fat and lazy. But they do raise some disquieting concerns about the future.

At the broadest level, Americans (in 1981) and Japanese (in 1985) spent their time in strikingly similar ways. Out of each 168-hour week, Americans on average devoted 56 hours to work, 70 hours to sleeping, eating, and other personal care, and 42 hours to leisure activities. Japanese allocated 56 hours to work, 72 to sleeping and other necessary activities, and 40 hours to everything else. At this level, life in Osaka looks much like life in Chicago.

TV GAP. But differences, some expected and some surprising, emerge when we peer below the surface. Take the breakdown of total work into work in the home and work for pay. The typical Japanese man devotes considerably more hours to his job than the typical American man (52 vs. 44, including commuting time). But he puts in vastly fewer hours at home (3.5 vs. 13.8). In total, American men worked about 2.3 hours a week more than Japanese men. Did you know that? I didn't. By the way, women in both countries put in almost exactly the same workweek: about 31 hours at home and 24 in the workplace.

The two peoples spent their leisure time

differently. A typical American's 41.8 hours of leisure per week broke down as follows: 16.3 hours socializing with friends or family, 12.1 hours watching TV, and the remaining 13.4 hours on all other leisure activities. The Japanese spent much less time socializing (on 7.5 hours), much more time watching TV (19 hours), and the same 13.4 hours on everything else. The puny amount of socializing may reflect the Japanese custom of concentrating such activities in the workplace. But think Americans can take solace in the data of couch potatoes. If Japanese television is as mind-numbing as American TV, we may yet win the competitive race. Stay tuned.

The numbers get worrisome when you look at the way schoolchildren allocated their time. During elementary school, Japanese kids spent 52% more hours in the classroom than American children. In junior high school and high school, the gap widened to about 60%. But the homework comparison was even more lopsided. In primary school, Japanese youngsters spent 8.3 hours a week studying, while American kids spent just 1.8 hours. In junior high school, the gap grew astonishingly, to 16 hours vs. 3.2 hours. And in high school, it was 19 hours vs. 3.8. In addition, Japanese kids spent two to three times as many hours reading as American kids did.

THE ROTE THING. If we count homework time and classroom time as equal and ignore outside reading, 12 years of Japanese education are equivalent (in terms of time spent) to 22 years of American education. Yes, I know we emphasize creativity and thinking while they emphasize rote learning, but 10.3 years does seem a big handicap—provided you wish to train a modern industrial work force rather than a legion of philosopher-poets.

The news is not all bad. Japanese children actually watch a bit more TV than American children, while our kids devote much more time to playing games and sports. Ours also sleep more. I score each of these comparisons in America's favor.

As ye sow, so shall ye reap. A recent survey of 16- to 65-year-olds in Oregon, a state that is certainly not at the bottom of the national literacy scale, found that only 12% of Oregonians could estimate the cost per ounce of peanut butter at \$1.59 a pound. Only 18% could use a bus schedule to determine the right bus to take from origin to destination at a prescribed time. But 97% could locate information in a sports article.

Think about this when next you sit by your TV watching great American athletes sandwiched between clever, American-made commercials selling high-quality Japanese cars.

ALAN S. BLINDER IS THE GORDON S. RENTSCHLER MEMORIAL PROFESSOR OF ECONOMICS AT PRINCETON AND THE AUTHOR OF *HARD HEADS*.
CONTINUED

The legends who compete in the Senior Open prove that golf is truly a lifetime game.

When a golfer like Arnold Palmer plays the seventy-two holes that make up the championship, he's just as charged up as he was at Cherry Hills in 1960 when he won the U.S. Open.

In 1980, the United States Golf Association established the Senior Open, recognizing the growing popularity of senior golf both at the amateur and the professional level. Six hundred thirty-one players entered the qualifying round for that first championship, which was played on the East Course of the famed Winged Foot Golf Club.

The champion was Roberto De Vincenzo, a national hero in his native Argentina and winner of the



Oakland Hills Country Club, site of the 1991 U.S. Senior Open

1967 British Open. De Vincenzo finished with a one over par score of 285.

The second Senior Open was won by another national hero, Arnold Palmer.



Arnold Palmer, winner of the 1981 U.S. Senior Open

Rolex and the Senior Open: The Classics Endure.

As "Arnie's Army" cheered from the sidelines, Palmer won a tense three-man play-off.

Today, the U.S. Senior Open ranks as one of golf's most anticipated events, both by the fans and by the players themselves. More than two thousand golfers entered this year's event.

Like Palmer, players in the Senior Open have a classic style—they continue to delight fans year after year.

Thus it's not surprising that so many players wear a classic—
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Economic Trends

BY MICHAEL J. MANDEL

WHEN THE GOING GETS TOUGH, THE TOUGH GET SELF-EMPLOYED

This recession is producing more than its share of budding entrepreneurs. Since last July, when the downturn started, the ranks of self-employed have swelled by some 240,000 people. Now, 8.97 million—almost 7.7% of all workers—are their own bosses, the highest level in 25 years.

Indeed, self-employment has been on the rise since the mid-1970s. More and more people, it seems, are willing to accept lower incomes and less security in return for more independence. New

ers who lose their jobs and start a new business can expect to take a pay cut of at least a third in the first year, reports David Evans, vice-president at NERA, an economic consulting firm. IRS tax figures paint an even bleaker picture: The average income of a business owned by one person was only \$13,871 in 1988, the latest year for which figures are available. When lawyers and doctors are excluded, this number falls to \$12,352. Even allowing for a substantial understatement of income among the self-employed, that's not very impressive. "It's a gritty type of existence," says Richard Belous, senior economist at the National Planning Assn., a Washington-based research group.

Still, regardless of the bad income prospects, self-employment is likely to keep rising, at least into 1992. It usually takes six months to set up your own business, say experts. So workers who were laid off in the fall are only now getting ready to strike out on their own. Indeed, if the 1981-82 recession is any guide, the peak of self-employment won't come until a year after the economy turns around.

MORE PEOPLE ARE WORKING FOR THEMSELVES



technologies such as faxes and powerful PCs make it easier to set up small businesses. And corporations are more eager to subcontract to lower-cost producers.

But much of the recent increase in self-employment has been, to say the least, involuntary. The downturn hit managers and professionals hard, especially in such industries as finance and retailing. Many of these laid-off workers count on generous severance packages and working spouses to cushion the financial risk of starting a new business. So far in 1991, some 16% of the clients at Right Associates, a Philadelphia outplacement company, are choosing to go solo after losing their corporate jobs.

But many of the new ventures may be short-lived. "A lot of people aren't cut out to go it alone," says James C. Cabrera, president of Drake Beam Morin Inc., a New York outplacement company. Many may start off undercapitalized, hurting their chances for success.

Even for successful startups, the financial rewards may be meager. Work-

ers who lose their jobs and start a new business can expect to take a pay cut of at least a third in the first year, reports David Evans, vice-president at NERA, an economic consulting firm. IRS tax figures paint an even bleaker picture: The average income of a business owned by one person was only \$13,871 in 1988, the latest year for which figures are available. When lawyers and doctors are excluded, this number falls to \$12,352. Even allowing for a substantial understatement of income among the self-employed, that's not very impressive. "It's a gritty type of existence," says Richard Belous, senior economist at the National Planning Assn., a Washington-based research group.

NOW THE REAL ESTATE SLUMP IS CLOBBERING INSURERS

The bad news about commercial real estate just keeps coming, and now it's life insurance companies that are being hit. In the first quarter of 1991, record 4.8% of the \$213 billion in commercial mortgage loans held by life insurance companies were delinquent by two months or more, according to a survey by the American Council of Life Insurance. That's up from 3% a year ago and 3.7% at the end of 1990. Indeed, the current delinquency rate has now exceeded the previous high set in 1976.

As bad as the overall numbers are, some regions are doing even worse. Besides the existing problems in New England and Texas, life insurers saw delinquency rates in the Mountain region, including Arizona, jump from 6.3% to 9.9% since the end of 1990. The East Coast, from New York to Florida, also showed a big increase in bad loans. According to Margaret M. Alexandre, an analyst at Salomon Brothers Inc., these real estate problems are likely to get worse in the next 12 to 18 months. So those life insurance companies with loans concentrated in the most depressed regions could be facing stiffer times.

WHY INNER-CITY JOBLESSNESS IS SO STUBBORN

Strong economic growth, according to most economists, was supposed to be powerful medicine for the problem of unemployment among inner-city young adults. As employers got desperate for scarce labor, the theory went, they would pull the idle from poor neighborhoods into the mainstream of the U.S. labor market. Alas, that's not what happened, even after the eight-year expansion of the 1980s. Unemployment for black males aged 20 to 24, for example, dropped only slightly, from 23.7% in 1980 to 20.2% in 1990. Since then, even this meager progress has disappeared, with their unemployment rate climbing back over 25% in April.

A new study from the National Bureau of Economic Research offers some insight into what went wrong. It suggests that poor young adults—even those with the potential for success—face surprisingly high barriers from peer pressure. Economists Anne C. Case and Lawrence F. Katz looked at 17-to-24-year-olds in Boston's poorest neighborhoods, both white and black, during 1989. They found that a young person was much more likely to be out of school and not working if family members and neighborhood peers also were idle. Move the same person into a different neigh-

TO BE YOUNG, RICH, AND BRIMMING WITH CONSUMER CONFIDENCE

In recent months, consumer confidence has stagnated, leading some economists to wonder whether consumers are ready to lead the economy out of recession. The Conference Board's Consumer Confidence Index has even fallen slightly, from 79.4 in April to 78 in June.

But one group, at least, is feeling much more optimistic: workers under 30 with above-average incomes. Their confidence has risen by almost 50% over the past couple of months, reports Stanley C. Plog, whose California-based marketing firm surveys 7,000 people each month. That's good news, since this group of successful young people, say Plog, is a bellwether for the rest of the economy.

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WAS BECOMING THIS SMALL.**



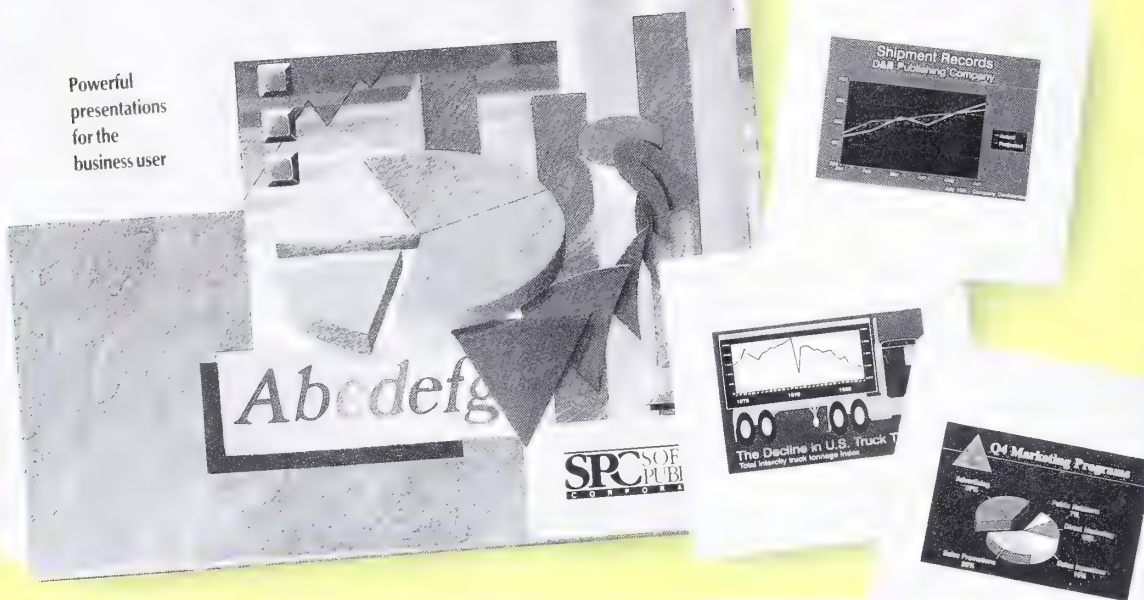
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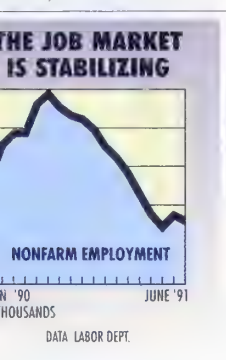


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THE NUMBERS SEEM AT ODDS, BUT THEY ADD UP TO RECOVERY

Don't worry too much if the recent economic data look like a mixed bag of pluses and minuses. That's exactly what they're supposed to look like in the trough of a business cycle, as different industries and regions emerge from recession at different times. In June, for example, employment decreased, but hours worked increased. In May, consumer credit fell, while retail sales rose. And May purchases of new homes declined, although housing starts advanced. On balance, the data continue to point toward recovery.



However, they do not answer the big question about what the upturn will look like. There are three scenarios: weak, strong, and short-lived. The consensus view favors a weak upturn accompanied by only modest inflation. Compared with past recoveries, when the economy posted first-year growth averaging about 6%, the real gross national product should increase only

1% during the next four quarters, with consumer prices rising just under 4%, according to economists in the July survey by *Blue Chip Economic Indicators*. Hanging your hat on the consensus view can be dangerous. It violates an old rule of forecasting—that the consensus is always wrong. And economists have tended to underestimate the strength of past recoveries. However, the numbers for May and June make a strong case that, this time, the consensus may be right.

THE JOBLESS MAY STAY LOCKED OUT

The June employment report was one of those mixed bags. Nonfarm businesses lengthened their workweek for the second consecutive month, to 34.5 hours from 34.3 hours in May and 34 hours in April. That's a classic recovery pattern. Companies typically add to their work time before bringing back laid-off employees.

Because of those increases, the drop in June payrolls is not so worrisome, but the failure of employment to keep expanding is a sign that the economy continues to struggle. Jobs fell by 50,000, after a revised gain of 100,000 in May. That increase was originally reported as 100,000, but hiring at stores and companies providing personal services was stronger than first thought. The June May advance could mean that April marked the trough for employment during the recession (chart).

The unemployment rate edged up from 6.9% in May to 7.1% in June—the highest since 1986. It would not be

surprising to see the jobless rate rise further this summer. Joblessness typically grows at the beginning of a recovery because the pickup in business activity draws more people into the labor markets before companies are ready to refill positions.

But this time, job seekers may be pounding the pavement longer than in past recoveries. Companies will have a stronger incentive to increase the hours of their workers and invest in new machinery rather than to add new employees. That's because businesses, particularly in the service sector, face an acute need to raise productivity of existing workers in order to cut costs and improve profitability, which has been sinking since 1989.

Because companies are stretching work hours, for example, the number of people holding part-time jobs has dropped sharply since April. However, that does little to take up the slack in the nation's labor pool.

PRICES AREN'T LIKELY TO LEAP

That slack—and the prospect that it will go away only slowly—is a big reason why wage growth is unlikely to fuel inflation in coming months. Average hourly earnings jumped 0.6% in June, but that partly reflects the month's big increase in overtime, which is paid at a higher rate. In the second quarter, wages were up only 3.4% from the same quarter of 1990. That's down from a 4% pace during the previous four quarters (chart).

The productivity gains that typically accompany recoveries will also help the outlook for inflation. Faster growth in productivity will offset the growth of wages and allow a slowdown in unit labor costs. That will give companies more pricing flexibility to repair damaged profit margins, but at the same time, lower unit costs will help hold back price hikes.

Looking outside the labor markets, it is also hard to see any fundamental upward pressure on prices. Commodity prices were still falling in late June. The stronger dollar is holding down import prices. And money growth is too slow to cause worry that it might fuel price hikes. Continued slack in the labor markets only assures the sanguine outlook for inflation.

Service industries, in particular, are wrestling with a productivity problem, because output per hour worked in this sector hardly budged during the second half of the 1980s. The hiring slowdown among service companies is

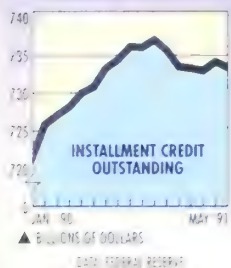


Business Outlook

the sharpest since the 1957-58 recession. During the past year, service jobs have declined by 0.4%.

Overall, the private service sector added 32,000 jobs in June, on top of the 62,000 added in May. But all of the June gain and most of the May increase came from the health care and business-service industries.

CONSUMERS LIGHTEN THEIR DEBT LOADS



Wholesale and retail trade and financial industries continued to lay off workers, although the workweek increased in all three sectors. Government jobs fell by 11,000 in June, and the fiscal troubles in many states and cities suggest further declines in coming months.

Manufacturers also continued to pare payrolls. Factory jobs slipped by 59,000, to 18.4 mil-

lion. That's the lowest payroll level in eight years. Payrolls in the machinery, electronics, and transportation-equipment industries took big hits last month.

The factory workweek, however, grew by 24 minutes, to 40.8 hours in June. Overtime increased to 3.7 hours from 3.4 hours in May. The rise in the workweek suggests that industrial output rose in June for the third consecutive month. However, a sustained advance in production will depend critically on consumer spending. And the slower companies are to add workers to their payrolls, the smaller the gains will be in consumer incomes.

CONSUMERS LOOK TO GET OUT OF HOCK

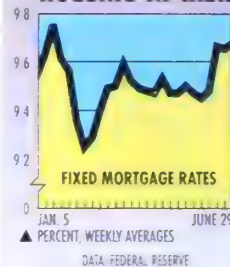
In the face of weak income growth, consumers have a real problem when it comes to leading the recovery. They have only meager resources to pay off their huge debts, rebuild their historically low savings, and find enough left over to spend. Judging by the latest report on consumer installment credit, reducing debt seems to be a top priority.

Consumers have paid off more debt than they took on in six of the past eight months (chart). In May, installment credit outstanding fell by \$626 million, to \$739 billion. Since last October, debt has fallen by an average of \$320 million per month.

Consumers seem especially determined to pay off the car loans. Auto credit has fallen in 14 of the past 17 months. And in May, car loans outstanding dropped by \$3.2 billion, the largest monthly decline on record. Revolving credit, largely charge cards, continued to expand in May, but even this category has slowed sharply. During the past year, revolving debt has grown 8%, compared with the 15% pace of a year ago.

Consumers' new distaste for debt probably reflects their persistent concerns about jobs and incomes. Against that backdrop, mortgage rates will probably have to be extremely attractive before people commit themselves to the purchase of a new home. The trouble is, fixed mortgage rates have risen, from 9.25% in late February to 9.67% in late June (chart).

RISING RATES PUT HOUSING AT RISK



Not surprisingly, sales of new single-family homes fell 3.3% in May, to an annual rate of 474,000, the lowest pace since January. The falloff was particularly sharp in the South. The drop raises new questions about how much lift the housing recovery will provide for the overall economy, particularly since the glut of existing apartment buildings is already exerting a record drag on overall housing starts.

To be sure, the data add up to a recovery. But until companies show more willingness to expand their payrolls, and until consumers prove that they have the wherewithal to support a lasting upturn, the modest expectations of the forecasting consensus seem justified.

THE WEEK AHEAD

BUSINESS INVENTORIES

Monday, July 15, 10 a.m.

Inventories at factories, wholesalers, and retailers likely fell by 0.5% in May, say economists polled by MMS International, a unit of McGraw-Hill Inc. Stockpiles also declined by 0.5% in April. Manufacturers have already reported cutting inventories by 0.8% in May.

INDUSTRIAL PRODUCTION

Tuesday, July 16, 9:15 a.m.

Output at the nation's factories, mines, and utilities probably increased by 0.5% in June, the same healthy gain as in May. That's suggested by the rise in total hours worked in the factory sector last month. Even with the expected

strong gain in June, output in the second quarter would be little changed from its level in the first quarter.

CAPACITY UTILIZATION

Tuesday, July 16, 9:15 a.m.

The projected advance in output suggests that operating rates for the industrial sector rose to 79% in June, according to the MMS report. In May, 78.7% of capacity was used.

HOUSING STARTS

Wednesday, July 17, 8:30 a.m.

The MMS consensus expects that housing starts stood at an annual rate of 1 million in June, a slight gain from the 982,000 pace of May. The dry weather in some regions increased building activity,

even though new-home sales are beginning to show some weakening.

CONSUMER PRICE INDEX

Wednesday, July 17, 8:30 a.m.

Consumer prices likely rose by 0.3% in June, the same mild increase as in May. Prices excluding food and energy are expected to rise just 0.3% in June also, following a 0.2% increase in May.

MERCHANDISE TRADE DEFICIT

Thursday, July 18, 8:30 a.m.

The foreign trade deficit probably narrowed to about \$4 billion in May, say the MMS economists. Exports and imports are expected to post declines, after both increased strongly in April. That month, the trade deficit was \$4.8 billion.



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JULY 22, 1991

OLD FRIENDS ARE BEST

ESPECIALLY AT THE FED—OR SO BUSH FIGURES

Although President Bush comes off as a pillar of the Eastern Establishment, he has always displayed a Texas-bred penchant for bank-bashing. So it's hardly surprising that almost from the day he entered the White House, Bush has grumbled about the Federal Reserve. The President and his lieutenants have used every weapon at their disposal—from barbs in State of the Union speeches to behind-the-scenes arm-twisting—to pressure the Fed to lower interest rates. Not that they got much for their efforts. Rather than hyping the economy, the Fed tried to slow growth into a "soft landing" that skidded instead into a recession.

So why did the President tap Alan Greenspan for a second four-year term as Federal Reserve Board chairman? For one thing, Bush sticks by people who stick with him. For all the White House grouching, Greenspan has kept any criticisms of Administration economic policy to himself. And even if he gets the blame for the recession, Greenspan can also claim credit for a recovery that got under way 18 months before the 1992 election. "I would not be standing here with this man if I did not have full confidence in him," Bush told reporters on July 10.

EYES ON THE POLLS. Can Greenspan keep Bush's confidence for four more years? The White House doesn't share Greenspan's goal of wiping out inflation by the mid-1990s. Bush wants to keep the recovery going, with lower interest rates when necessary, and he'll expect Greenspan to deliver, even though the Fed has grown increasingly fractious. But reappointment, particularly once the 1992 election is over, could give Greenspan the freedom to follow his lifelong belief that sound money and low inflation are the best way to guarantee steady growth.

That dyed-in-the-pinstripes, central banker attitude was responsible for Greenspan's mistakes during his first term. Greenspan's greatest triumph was

to keep the aging economic expansion going through the 1987 stock market crash. But he admits that he was caught off-guard when banks choked off business lending last summer. Greenspan still argues that the recession began in October, months after Saddam Hussein's invasion of Kuwait. That puts him at odds, however, with the official business-cycle arbiters, who date the slump to July. Although the Administration doesn't buy Greenspan's argument, a top Bush aide says "no one would argue that Greenspan exclusively caused" the slump.

Such faint praise reflects some White House ambivalence about keeping Greenspan. But the internal debate that preceded the decision was brief and mild. Treasury Secretary Nicholas F. Brady briefly championed E. Gerald Corrigan, who has impressed Brady's Wall Street friends during six years as president of the New York Fed. But other aides, including Budget Director Richard G. Darman, argued that Corrigan is an inflation hardliner like his mentor, former Fed Chairman Paul A. Volcker. Corrigan also opposes key elements of Brady's own bank-reform plan. Eventually, aides realized that their dissatisfaction wasn't strong enough to overcome Greenspan's ties to Bush.

While they couldn't block Greenspan, Bush aides used delay over reappointment to squeeze him. The tactic may have worked: At the July 2-3 meeting of the Fed's Open Market Committee, the panel left its targets for M2 money-supply growth unchanged for next year. Greenspan has cut those targets in three



DESPITE THE RECESSION GREENSPAN HAS LIVED TO BUSH'S EXPECTATIONS

THE GREENSPAN RECORD

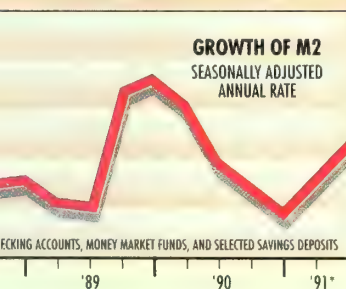
DATA: FEDERAL RESERVE, COMMERCE DEPT., BW ESTIMATE

of the past four years, and lower 1992 targets would fit with his long-term strategy of reducing inflation to zero. Fed officials note the decision could be changed once the economy's strength becomes clearer. But, adds a senior Fed official, "we also had to look at where we are in the chairman-selection cycle."

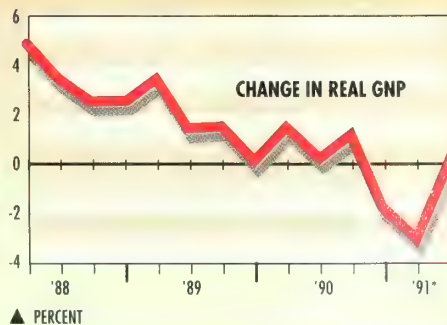
A steady rebound would work wonders for White House-Fed relations.



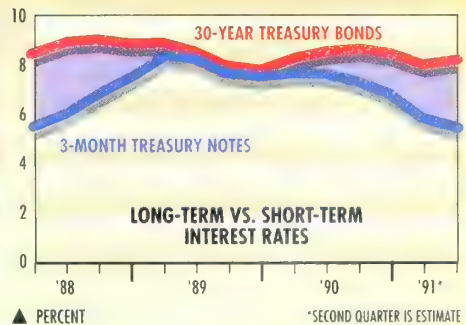
HOLDING DOWN MONEY GROWTH...



...HAS SLOWED THE ECONOMY...



...BUT INFLATION FEARS KEEP LONG RATES HIGH



th the recession "barely cold in its
ve," a senior Administration official
ts that "it's very important that the
d not follow a policy that prematurely
uffs out the recovery." But most fore-
sters—including the Fed—see growth
only about 3% for the next year, with
flation falling. The Fed may have no
son to raise rates for months.
The honeymoon may not last, though.

Next summer—in the heat of the 1992
Presidential campaign—the Fed may
have to decide whether to increase rates
to meet its goal of "price stability" by
the mid-1990s. Greenspan believes that
controlling inflation "is a necessary con-
dition to maximizing growth and employ-
ment." But cutting inflation may require
years of below-par growth and high un-
employment. To a public inured to 4%

annual price hikes, that cost may well
seem too high. Greenspan sidestepped
those concerns in his first term. The
Fed's goal then was a gradual squeeze,
presented as the best way to correct the
excesses of the Eighties. But if the econ-
omy shows signs of flagging, any kind
of squeeze will be tougher. If Greenspan
persists in seeking price stability, "he'll
risk being so far out of step he'll put the

Fed's independence in jeopardy," warns H. Erich Heinemann, chief economist at brokers Ladenburg, Thalmann & Co.

Continued turmoil in banking may also force the chairman to tread lightly. The financial system made it through the recession without a major crisis. But many banks are still bleeding from bad loans. Neither the credit crunch nor the threat of major failures is behind the banking system.

To avoid being blindsided again, Greenspan is spreading his intelligence net wider. He still watches such financial indicators as money supply growth (charts). But those signals will become harder to read as the financial industry evolves, a process that will accelerate sharply if Congress passes sweeping bank-reform legislation. So Greenspan has stepped up surveillance of lending and is paying more attention to anecdotal evidence about credit conditions. That, says former Fed Governor Lyle E. Gramley, "will be crucial to staying on top of the economy."

Meeting that challenge will require stronger leadership than the cerebral Greenspan has shown to date. He has allowed a debate to rage between Fed traditionalists, who are vigilant about inflation, and superhawks, who are willing to put the economy through the wringer. Greenspan's reluctance to knock heads could lead the Fed to tighten earlier than either he or the White House would like. "Most people in the [Fed] system like Alan's style," says a former official. "But he doesn't have the sort of fear-respect thing a chairman needs."

SECOND CHANCE. Democracy within the Fed has produced some embarrassments. In mid-April, for example, Greenspan wanted to cut the discount rate, but he had only one other vote on the Fed board. So the Fed chairman let Treasury Secretary Brady, who was trying unsuccessfully to persuade U.S. allies to reduce rates in concert, to lobby Fed governors for the cut. When the Fed's move finally came, it "came across as 75% political on Greenspan's part," says David M. Jones, chief economist at Aubrey G. Lanston & Co.

A second term will offer the 65-year-old Greenspan a chance to go down in history as the man who restored the brief, shining era of the mid-1960s, when the economy enjoyed steady growth and low inflation. But Greenspan is also loyal to the Republican Party, which could need a more vibrant economy to hold on to the White House. That conflict between historical possibility and political reality will weigh on every decision he'll make in the next four years.

By Mike McNamee, with Douglas Harbrecht, in Washington

SOFTWARE

'ASHTON-TATE IS NOT AN ACTIVE FORCE ANYMORE'

Archival Borland has agreed to acquire it in a \$439 million stock swap

It's the latest example of the old business maxim: Grow or die. In 1988, Ashton-Tate Corp. was a \$307 million-a-year company, renowned for its dBase software, which stores and manages information on personal computers. Borland International Inc., also a software maker, was just one-third its size. But then, the bigger company stumbled in getting new products to market, sales plummeted, and Borland moved in to take advantage. Borland began cutting into Ashton-Tate's lead, then caught up in size. Just this May, Borland's chairman and founder, Philippe Kahn, proclaimed that "Ashton-Tate is not an active force anymore."

At least not under its own steam. On July 10, Borland announced an agreement to acquire its rival in a \$439 million stock swap. For Kahn, the deal provides the industry clout he has long coveted. With the merger, Borland doubles its revenues, to around \$500 million, and becomes the No. 1 maker of data-base software in the PC industry. The deal also places Borland among the top five



KAHN MUST MELD INCOMPATIBLE DATA-BASE PRODUCTS

makers of all PC software. Most important, the new company's might will help blunt Microsoft Corp.'s expected entry into the data-base market and create a scrappy challenger to rival Oracle Systems Corp. "It's a very strong move," says Marc R. Benioff, Oracle's vice-president of marketing.

PAIN FIRST. The acquisition brings risks. In the short term, Borland stands to lose sales. Since both companies sell data-base software, customers may hold back on purchasing products from either company until the deal is completed several months from now, pending government and shareholder approval. "Customers

will wait until the dust settles," says Chuck Taylor, an analyst with Needham & Co. He points to the unfortunate example of Computer Associates International Inc. After that company bought two data-base software companies back-to-back in 1988 and 1989, many customers delayed purchasing decisions for up to a year while the company explained how its new products fit together. The delays brought its first losses.

And Kahn must move quickly to streamline costs. That could prove especially painful for "Taters," as Ashton-Tate employees dub themselves, since they will become merely part of a division at Borland and are most likely to suffer any cost cuts. With Kahn running the merged company, William Lyons, chief executive at Ashton-Tate, is expected to resign after a transition. The two sides have already agreed on Borland's Scotts Valley (Calif.) home as headquarters. Analysts expect deep cuts by Borland—perhaps as many as 600 layoffs, or about 35% of Ashton-Tate's work force.

WHAT EACH SIDE BRINGS TO THE PARTY

	ASHTON-TATE	BORLAND
FOUNDED	1980	1983
1990 REVENUES	\$231 million	\$226 million
1990 NET INCOME	-\$18 million	\$27 million
EMPLOYEES	1,750	1,000
SHARE OF DATA-BASE MARKET	45%	20%
OTHER PRODUCTS	Graphics Word processing	Spreadsheets Programming tools

DATA: COMPANY REPORTS

Things began to fall apart for Ashton-Tate in October, 1988, when it started shipping a vital new version of its flagship dBase software. "We're pleased to have met our quality standards," said Chief Executive Edward M. Esber Jr. as he announced the product. Little did he know that the program was crawling with so many bugs that many customers could refuse to use it. The product was recalled, and developers got to work on fixing it. Before they were through, however, the company's sales went into a nosedive, and Ashton-Tate reported 20 years of losses. Esber was forced to resign in April, 1990, three months before Ashton-Tate delivered the patched-up software. Since then, the company has returned to profitability, but not to the industry stature it once held.

VERSATILE FRENCHMAN. Borland thrived on Ashton-Tate's slipups. It offered its dBase 5 Paradox data base to dBase customers for only \$150. In addition to undercutting Ashton-Tate on pricing, Borland became the first company to sell mainstream business software using direct mail. Its aggressive direct-marketing campaign brought it nearly 20% of the PC data-base market. Much of Borland's success was attributable to Kahn, a sailing buff and saxophonist who left his native France to start the company. Like Microsoft's William Gates, Kahn has a knack for both business and technology. Although he must manage 1,000 employees, he still finds time for examining computer code and explaining technology to customers.

Now, Kahn may have a lot of explaining to do. Borland and Ashton-Tate sell incompatible data-base products. "If you look at the two technologies, they're not going to mix together very easily," says Larry M. Heimendinger, president of rival Nantucket Corp. Kahn has already unveiled a strategy to meld the two product lines together over time. He is banking on a technique called "object-oriented" programming that allows different software programs to work together interchangeably. But many customers aren't familiar with the technology and are likely to be skeptical. Meanwhile, Oracle and Microsoft can swoop in.

If Kahn can work out the details, though, the companies make a compelling combination. Ten-year-old Ashton-Tate has a loyal legion of more than a million customers and consultants. They know how to tailor Ashton-Tate's flagship dBase software so it can do anything from managing medical records to controlling corporate payrolls. As long as Kahn doesn't disappoint those customers the way Ashton-Tate did, growth could be no problem.

By Evan I. Schwartz in New York, with Richard Brandt in San Francisco

SAY, DOES WORKERS' COMP COVER WRETCHED EXCESS?

California wants to ban mental-stress claims by fired employees

Layoffs are never easy for small manufacturers such as Security Metal Products Corp. But the Hawthorne (Calif.) metal-door maker is finding layoffs especially painful these days. Thirty percent of the workers the company has laid off over the last few years have claimed mental stress and filed claims for as much as \$25,000, says David B. Hirsch, vice-president for operations. Security's insurance company typically settled up fast, for as much as \$10,000. "The way the law was written, we couldn't win by fighting them," Hirsch says. He has since moved most of his company, which currently employs 125 people, to Oklahoma, where the law is less hospitable to stress claims and overall costs are considerably lower.

Hirsch is not the first executive to discover that stress claims have become a growth industry in California. Last year alone, an estimated \$380 million was paid to employed and unemployed workers claiming sleepless nights, headaches, and other ills. TV commercials and newspaper ads beckon workers to doctors and lawyers, who counsel those employees who have been fired, transferred, or work under unusual pressure. Plenty of other states are struggling to cap the costs of rising workers' compensation claims. But in California, stress-related claims have now become the key issue in resolving the already convoluted struggle over the state's \$56 billion budget.

QUID PRO QUO? Even though tighter restrictions on stress claims wouldn't raise a dime toward the additional \$2.3 billion the state needs to close its budget gap in timely fashion, Republican Governor Pete Wilson says such measures must be part of the budget package. "Workers' compensation has become a major cost of doing business in California and is a disincentive for companies to expand in or move to California and create jobs," the governor says. His proposal would make workers prove that their jobs contributed to 50% of their mental stress, up from the current 10% require-

ment. Wilson would also disallow all claims for stress attributable to firings or layoffs.

California Democrats and unions charge that Wilson, who is backed by the state's largest business groups, is making tougher laws on workers' compensation the price for agreeing to a tax hike on businesses and the wealthy. "The condition for taxing the rich is screwing the workers," blasts Assembly Speaker Willie L. Brown Jr. And labor, which had hoped to push legislation next year to raise California's current \$336-a-week disability limit, sees the recent

turn of events as the first move toward scaling back the state's overall workers' compensation program.

Even if the fight over mental stress claims is only symbolic, few would deny that California's workers' compensation program has problems. According to an industry group, the National Council on Compensation Insurance, Golden State workers collected \$5.3 billion in disability payments in 1989, the last year for which numbers are available. That's roughly a 10% hike over

the previous year. As a result, California companies pay insurance rates second only to Montana, which is dominated by riskier industries such as mining and timber (chart).

California is only one of four states to allow claims for stress, but the present fight may well be the precursor of state-by-state battles to cut back on workers' compensation programs in general. In Maine, 10,000 workers were temporarily furloughed earlier this year when Governor John R. McKernan Jr. and Democratic legislators fought over budget cuts that included payments in the workers' compensation program. Pennsylvania is also looking into cutting workers' comp, says Richard A. Victor, executive director of the industry-supported Workers' Compensation Research Institute. At that rate, the David Hirsches of the world may soon find more and more states beckoning as factory sites.

By Ronald Grover in Los Angeles



NOT WITH OUR GAMES YOU DON'T

The pro athletic leagues are fighting against state-run sports lotteries

Lawmakers may not know much, but they're sure of one thing: People would rather gamble than pay taxes. In the past few years, as voters balked at new levies, 33 states and the District of Columbia bet that lotteries would spin off millions of dollars in new revenues. They bet right: The games netted states \$7.8 billion last year.

Now, with dozens of states facing budget crises, legislatures may add a new wrinkle to legalized wagering: rewards for picking the winners of professional sports contests. Oregon has had such a lottery for two years, with the proceeds earmarked for the state university system's athletic programs, and other states may soon follow suit. That could spark a bitter legal brawl with the major professional sports leagues, which back federal legislation that would bar sports lotteries. A Senate Judiciary subcommittee is scheduled to vote on such a bill on July 17.

SHOELESS' SHADOW. The states do need a financial home run. Thirty of them, plus the District and Puerto Rico, ran deficits in the last fiscal year, and many took drastic steps when their new fiscal year started July 1. Several governors ordered cuts in payrolls, and Connecticut and Maine temporarily halted state services.

To help plug their budget gaps, legislatures in Illinois, New York, Pennsylvania, and other states are mulling bills that would authorize state-sponsored sports betting (table). And in California, signatures are being gathered for a ballot initiative that would permit such a lottery there. Many more states are awaiting the outcome. "If we can get a game started in a major state, with revenues meeting our projections, more people will take a harder look," says William S. Bergman, executive director of the North American Association of State & Provincial Lotteries.

That prospect terrifies the professional sports leagues. Although newspapers across the country print point spreads and betting lines,

league executives worry that legalized gambling would just give teenagers further encouragement to gamble. "The problem is so bad already, we don't need to make it any worse," says Valerie C. Lorenz, director of the National Center for Pathological Gambling.

The pros also worry about resurrecting memories of the Black Sox scandal, in which several Chicago White Sox players took payoffs from gamblers to throw the 1919 World Series. "Gambling threatens the integrity of, and public

confidence in, all sports," declares National Basketball Assn. Commissioner David J. Stern. Big-time sports can hardly afford another embarrassment in the wake of repeated drug scandals and the Pete Rose gambling affair.

Illegal sports wagering, say league officials, is already too pervasive. Government approval, they contend, would only make matters worse. "The game's integrity would be open to question play by play, day after day," says baseball Commissioner Fay Vincent.

Those fears haven't deterred legislators, even though the take from sports lotteries might not amount to much. Oregon's football-based Sports Action game netted a paltry \$1.6 million last year. The minimum wager is \$2 on at least three games, and the prize is \$10 for picking three winners and \$20 for choosing four. The payoff for picking more than four winners—and no losers—depends on the wagering pool and the number of winning bets.

TIED HANDS. Some experts believe that sports lotteries could be more profitable in larger states with more pro franchises to boost fan interest.

Others contend that sports lotteries would simply divert money from existing lottery games, rather than bring in new money. But for some state lawmakers, the size of the lottery handle isn't the only issue. While the recession is largely responsible for the states' fiscal woes, state officials are peeved that they've had to pick up an ever-growing portion of the tab for health and other services. "The federal government has shifted billions of dollars in new responsibility to us, and at the same time they want to restrict our sources of revenue," fumes Kansas State Representative Wanda L. Fuller (R-Wichita).

Even if the states win the political battle in Washington, they're not assured of victory. In 1989, the NBA sued Oregon, charging that the lottery violated the league's trademark rights to its games. The state, whose only pro sports franchise is a basketball team, agreed to remove NBA results from its lottery, and the league dropped the suit. The Oregon game now is limited to football. If football lotteries spread to other states, though, the National Football League is prepared to blitz. "We're not ruling out any legal avenue," says an NFL spokesman.

With the stakes so high, both the states and the leagues are wearing their game faces. Congress and the courts have some tough calls ahead.

By Peter Hong in Washington



OREGON'S LOTTERY TAKE GOES TO ITS UNIVERSITIES

TO BET OR NOT TO BET

STATES MULL SPORTS WAGERING

ILLINOIS	The state senate is considering a bill permitting a sports lottery based solely on the outcome of Chicago sporting events
NEW YORK	The state assembly is considering two bills authorizing pari-mutuel betting on the scores of professional contests
PENNSYLVANIA	A bill to establish a sports betting pool is working its way through the state legislature

DATA: NORTH AMERICAN ASSOCIATION OF STATE & PROVINCIAL LOTTERIES

IBM AND APPLE: CAN TWO LONERS LEARN TO SAY 'TEAMWORK'?

The deal was done with little fanfare: There was no press conference with flashing strobes and television cameras, no meeting with Wall Street's pundits, no explanation to customers. Instead, the day before America took off for the Fourth of July holiday, IBM Corp. and Apple Computer Inc. issued a few paragraphs briefly summarizing the most dramatic alliance in the personal computer industry's short history.

IBM says it is keeping mum because the deal, which calls for extensive technology sharing between the two former rivals, is only tentative. Final contracts won't be signed until later this year. "What we've done is outline the areas of discussion," says Joseph Guglielmi, an IBM vice-president. "It will raise hundreds of questions."

NOTHING GAINED. That's for sure. One of the first questions is whether the alliance will actually lead to much. After all, Big Blue has a history of high-profile agreements that fizzled before they delivered anything. Among its most notable: The \$1.25 billion acquisition of telecommunications giant Rolm Corp. in 1984. IBM hinted that that buyout would give it the leverage to outdo American Telephone & Telegraph Co. But after repeated difficulties in integrating Rolm's wares into IBM's product line, Big Blue sold most of Rolm to Siemens in 1989.

But IBM in 1991 isn't the IBM of 1984. When it did its deal with Rolm, Big Blue was at the top of its game, and its imperial management style made integration of the two nearly impossible. Now, IBM is desperately trying to stem market-share erosion and profit decline and to boost stagnant revenues. That has created an IBM willing to swallow its pride and turn to outsiders for help. That augurs well for the partnership, as long as Apple can overcome its long-running hostility to IBM and show an interest in team-

work. For IBM, the Apple deal is just the latest in a series of alliances aimed at moving IBM quickly into the 1990s by giving it access to important new technologies (table).

IBM's crisis-inspired cooperative spirit is just what's needed to make its deal with Apple—and the others—successful. For now, the two companies aren't making any pledges they can't keep. The world's No. 1 and No. 2 PC makers,

which provides a PC's basic instructions. That's clearly targeted at unseating Microsoft Corp., an IBM partner turned rival, from its role as the primary provider of such software.

With the deal, IBM also has a good shot at displacing its most nettlesome PC competitor, Compaq Computer Corp. The agreement gives Apple access to IBM's reduced instruction-set computing (RISC) chip. Apple will leverage the silicon deal to advance into workstations. Those products will throw weight behind IBM's RISC, which it uses in its RS/6000 computer, and hurt attempts by Compaq to create a standard with another RISC chip.

And if all that isn't enough to keep IBM collaborating happily with Apple, there's another aspect that probably will: the threat from Japan. The two companies plan to jointly develop multimedia—the integration of video and sound with computer text. Multimedia is expected to be a hot button this decade, and a razzle-dazzle product from IBM and Apple would throw cold water on Japanese attempts to come up with similar machines. Just the threat of the deal will likely endanger one such effort: Although Apple never formally admitted to the relationship, it had been working with Sony Corp. on multimedia.

Long-term, IBM wants to do more than trump Microsoft, Compaq, or the

Japanese. IBM wants to pull out of its well-documented malaise by wresting control of the personal computer. The goal? A return to its PC glory days of the early 1980s, when its technology set the industry's agenda.

To do so, IBM must invest in its own research—it can't farm out innovation forever. Still, if it can set aside its haughtiness and resist the temptation to overwhelm Apple and its other partners with bureaucracy and advice, it may find itself in the driver's seat.



PC PALS: BIG BLUE HAS A HISTORY OF HIGH-PROFILE VENTURES GONE AWRY

IBM'S NEW ALLIES

Partner/Date deal struck	Purpose
GO /July, 1990	Handwriting-recognition software
METAPHOR /September, 1990	Operating system development
NOVELL /February, 1991	Rights to networking software
BORLAND /May, 1991	Rights to software development tools
WANG /June, 1991	Access to imaging technology
LOTUS /June, 1991	Access to electronic mail technology
APPLE /July, 1991	Extensive technology collaboration

DATA: BW

which combined have 38% of the \$93 billion PC market, promise only to create new computers "for the 1990s."

Both clearly plan to do more. Their goals are impressive: Under the agreement's terms, IBM and Apple plan to jointly develop software that will make it easier to link Apple and IBM computers on networks. That will help Apple move more aggressively into big corporate accounts. And the two have also agreed to form a joint venture to develop new operating system software,

CHIPPING AWAY AT FRITO-LAY

The snack maker is still No. 1, but hungry rivals are forcing a shakeup

Over the past decade, Roger A. Enrico has been on the front lines of the cola wars. The charismatic Pepsi-Cola chief, with advertising help from the likes of Michael Jackson and Madonna, narrowed the market-share gap between Pepsi and industry leader Coca-Cola.

Nowadays, Enrico finds himself on the other side of the fence. After seven months as chairman of Frito-Lay Inc., PepsiCo Inc.'s most profitable unit, he is becoming quite familiar with feeling hungry competitors on his heels. With more than 40% of the \$12.6 billion U.S. market for salty snacks, Frito is in no danger of toppling from the No. 1 spot. But under pressure from a growing roster of national players and more value-conscious consumers, Enrico is overhauling the \$3.5 billion company. Vows Enrico: "We're going to make a major change in the way we manage this company."

DISCOUNT FRENZY. Enrico, whose first PepsiCo job was as associate product manager at Frito-Lay in 1971, is already starting. He has slashed prices to come within striking distance of discounting competitors, primarily Anheuser-Busch Cos., whose Eagle Snacks Inc. unit is the country's fastest-growing snack-food maker. So far, analysts say, Eagle's gains haven't come at Frito's expense. But "Eagle is a concern," says Enrico. "Not for what they are now but for what they have the potential to become." The battle has taken its toll on Frito's bottom line (chart). First-quarter operating profits of \$133 million were down slightly from a year earlier on sales of \$814.6 million, a gain of 11%.

The discounting frenzy isn't likely to let up soon. Despite its premium image, Frito can no longer enjoy the luxury of premium pricing. For instance, before the price wars, a bag of Lay's potato chips could cost as much as 15% to 20%

more than the competition's. "Consumers are more quality- and value-conscious than ever before," says Enrico. He now has to give shoppers more for their money. And he'll spend as much this year on quality improvement—such as upgrading raw materials and cutting down on the number of broken chips in a



ENRICO PROMISES "A MAJOR CHANGE IN THE WAY WE MANAGE THIS COMPANY"

bag of Ruffles—as Frito did in the last seven years combined.

He'll also exploit his company's dominance of the market. The cornerstone of this strategy: new products, new sales outlets, new machines. He'll sell offerings such as multigrain Sunchips through broader distribution channels, including the fast-growing warehouse clubs, and he'll make the chips in more efficient factories.

All those changes require shaking up Frito's highly stratified bureaucracy. For help, Enrico has called in consultants McKinsey & Co. to review operations at Frito's Plano (Tex.) headquarters and four field offices. The study will focus only

on Frito's 3,000 management, administrative, and professional positions. Analysts say layoffs, possibly as many as 400 to 600, and a write-down are likely after the study ends in September. Enrico isn't offering any estimates on the review's results, but he says they're "not going to be insignificant." He spearheaded a similar streamlining at Pepsi, writing off a total of \$26.8 million for decentralization of domestic and international operations. "He's prone to shake things up a bit," says Joseph J. Doyle, an analyst with Smith Barney Harris Upham & Co. in New York.

ROOM TO IMPROVE. For Frito, grabbing market-share gains won't be a snap. Aggressive competitors such as Eagle

Snacks are coming on strong. "We've been picking up a lot of shelf space," says Eagle Snacks President Kevin F. Bowler. And Keebler Co.'s new grain-based Pizzaria chips are competing head-to-head with Frito's Sunchips, which were a hit in test markets.

Getting significant efficiency gains out of factories and the distribution system will be quite a feat for what's already a tightly run operation. Frito's 40 plants produce 10,000 packages of snacks per minute. And the company's 10,000-strong sales force uses handheld computers to pinpoint

stores where sales are stronger or weaker than expected.

The new boss insists there's room for improvement, though. Enrico predicts he can save \$75 million annually if he makes bigger deliveries to just a few high-volume accounts. He also figures he stands to gain by relying on fewer

suppliers and working more closely with those that are left.

As the new strategy kicks in at Frito, its chief says that the company "won't be as predictable as it was before." Considering Enrico's handiwork at Pepsi-Cola, that's probably a safe prediction.

By Stephanie Anderson Forest in Plano, Tex., with Julie Flynn Siler in Chicago



THE POLITICS OF PHONE FAILURE

The Bells say outages show why they should make equipment

The massive network failures that knocked out most local telephone service in Washington, D. C., surrounding states, and Los Angeles last month weren't anything for the phone companies to brag about. But some resourceful lobbyists allied with the Baby Bells think they've found a way to turn such disasters to their advantage. They argue that the outages—traced to programming errors in a supplier's software—show why the Baby Bells should be permitted to design and manufacture their own telecommunications gear.

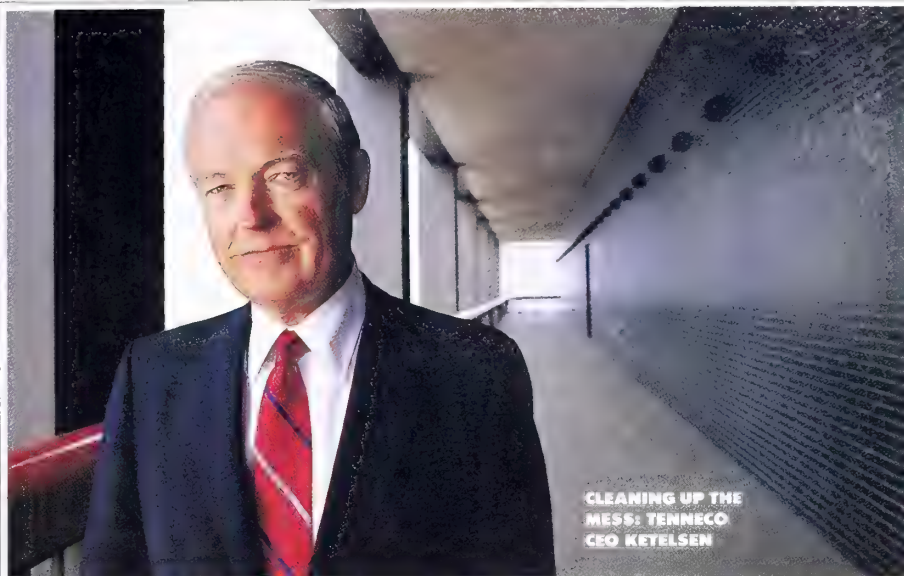
The seven regional Bells have long lobbied against the manufacturing ban contained in the consent decree that broke up American Telephone & Telegraph Co. in 1984. They say that the restriction retards the development of new equipment needed to keep the U. S. at front in telecommunications.

CROSSED WIRES. The failure of signaling networks at Bell Atlantic Corp. and Pacific Telesis Group plays into the hands of the pro-manufacturing forces. It shows the importance of close cooperation between phone companies and equipment makers. The failures may prompt Congress to pass, and President Bush to sign, a long-delayed bill that would allow the Bells to make equipment. Supporters of the bill argue that the Bells must be freed from the "judicial tyranny" of U. S. District Court Judge Harold H. Greene, who monitors them for antitrust behavior.

But the phone disaster may not produce as many lobbying dividends as the Bells and their backers would wish. That's because Greene, despite being labeled an obstructionist, ruled on July 10 that Bell Atlantic was perfectly free to operate with its supplier, DSC Communications Corp., on diagnosing and solving the software problems in the errant switches. And he noted that there was absolutely nothing in the decree that would keep the Bells from rigorously testing products they buy from DSC and others. His decision undermined the argument that Greene alone stands between the Bells and a secure telecommunications network.

The recent snafus may not end up paying off for the Bells. But, once more, whatever happens in Washington seems to create an opening for someone.

By Peter Coy in New York



CLEANING UP THE MESS: TENNECO CEO KETELSEN

AS J.I. CASE SOWED, SO SHALL IT REAP

It glutted dealers with farm machines. Now, they're selling at a loss

James K. Ashford seemed to have the magic touch. In 1987, he took over as president of J. I. Case Co., Tenneco's troubled farm-equipment division, and turned it into a powerhouse. Under Ashford, Case churned out electronics-packed tractors that farmers happily paid \$80,000 to own. In 1989, Case earned a stellar \$228 million, and he seemed likely to succeed James L. Ketelsen as CEO of Tenneco Inc. But in March, just three months after being named a Tenneco director, Ashford abruptly resigned. Says a former Case executive: "No one could figure it out."

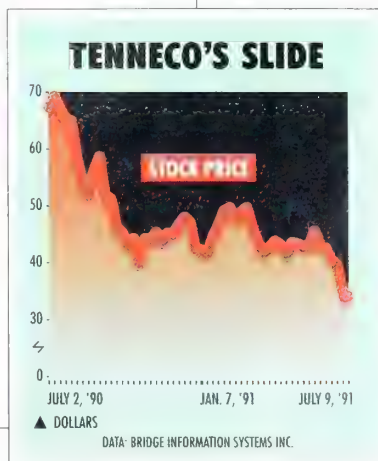
Now, the reasons for his sudden departure are becoming clearer. In an effort to boost performance, Ashford may have left Case especially vulnerable to a downturn. While other suppliers were cutting back production late last year, Ashford kept on shipping—booking strong annual sales of \$5.4 billion but leaving its dealers swamped with inventory in a recession. Case had to unload the machinery at fire-sale prices—and take first-half losses estimated at \$247 million. The red ink is still flowing, and it may take a sale of part of Case to help staunch it. "They're paying for last year's sins," claims a former

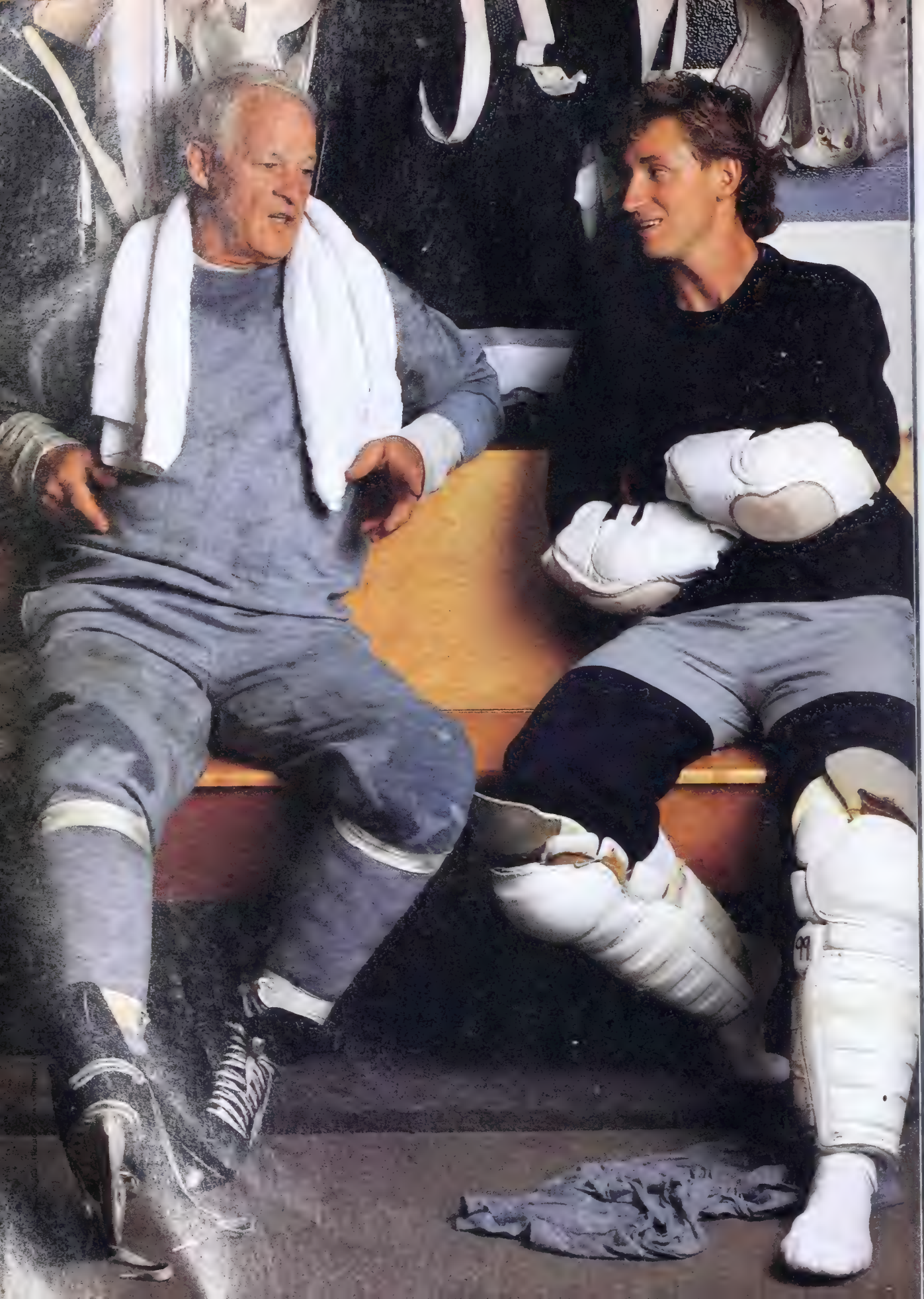
company executive. "It was all smoke."

Ketelsen and Ashford say there was nothing wrong with Case's sales practices. But neither man denies that Case's problems are hammering Tenneco. C. J. Lawrence Inc. analyst Paul J. Milbauer estimates that the Houston conglomerate will be lucky to make \$100 million this year, down from \$561 million in 1990 on sales of \$14.5 billion. At 34%, Tenneco shares are trading at half their year-ago level (chart). "The wolf's at the door," says Milbauer.

DICEY NUMBERS. Those dire straits must seem familiar to Ketelsen, an Iowa native who ran Case in the late 1960s. When he tapped Ashford to take over Case, it was struggling to absorb the farm-equipment operations of International Harvester, which it bought in 1985 for \$475 million. Ashford, who had just engineered a turnaround of Tenneco's automotive-parts unit, slashed the work force by 10%, to 27,000, shuttered four plants, and cut back on discounting, reducing overall costs by \$150 million a year. He also caught a break: The seven-year agricultural recession ended just as he was taking over.

Ashford did, however, continue one longtime Case practice. The company, like





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other farm equipment manufacturers, books the sale when it ships a piece of equipment to a dealer—even though it doesn't get paid until the dealer sells the goods, often at a discount. Some Case rivals, such as Deere & Co., immediately adjust sales figures downward by as much as 20% off their list prices. By comparison, Case often adjusted downward by a much smaller percentage, say former executives of the company.

The practice conforms to generally accepted accounting principles, which provide flexibility. But it's risky. And Case's aggressive accounting continued even as the market was slowing last year, say those former executives.

FURROWED BROWS. The strategy began to go sour when Iraq invaded Kuwait in August and showroom traffic dried up. Case compounded its woes by continuing to ship tractors through December. While Deere cut back U.S. production 21% in the last quarter, "we just kept shipping tons of equipment," says a former executive. Says another: "They tried to sell their way out of it, and it didn't work." Ketelsen responds: "By the time we knew where we were in August, it was October. We figured [the market would] settle down sooner."

In any event, the subsidiary came into 1991 with nearly 11 months' worth of inventory, vs. 7 for the industry and 3 or 4 for Deere. Just before the start of the second quarter, Ashford resigned, for "personal reasons."

Now, Ketelsen has to clean up the mess. He has cut production by 25%, laid off 4,000 workers, and given dealers rebates and incentives that reduce prices on some tractors by as much as 35%. But while Case sales are rising again, Deere continues to dominate the market for large farm machines, with a 42% share, vs. 32% for Case, says John A. Stark, who publishes an industry newsletter. Nor are Tenneco's other businesses helping. Operating income at its gas-pipeline, shipbuilding, and other operations will be down 7% this year, to \$1.1 billion, says Ronald J. Barone, a Kidder, Peabody & Co. analyst.

Meanwhile, Tenneco's costs and debt are rising. Barring a roaring economic recovery, Barone figures Tenneco will have a cash-flow deficit of nearly \$600 million for 1991.

Ultimately, Ketelsen may have to sell Case—or at least part of it. Case dealers say he's shopping Case's construction-equipment unit to Japan's Kubota Ltd. Ketelsen refutes that report—and speculation that he may leave soon. "I'm going to be here a while," he vows. Case's problems aren't going anywhere, either.

By *Michael J. Perry* in Houston and *Kevin Kelly* in Chicago

TO: ALL READERS SUBJECT: CORNER-OFFICE SOUND-OFFS

What to do when you feel like issuing an all-points chewing-out

It's taught in all the best business schools: If you have an unpleasant message for your employees, don't send a memo. So much for lessons learned in B-school. These days, stinging memos are everywhere. From the nooks and crannies of Big Blue to the four corners of the Magic Kingdom, they're appearing more and more in photocopies slipped into "in" boxes or as blinking messages in electronic-mail queues. Sometimes they even appear excerpted in newspapers and magazines.

Most often, the message is grim: Business is bad, and it's your fault. IBM Chief Executive John F.

Akers asked the troops what they had done for him lately. Microsoft Corp. Chairman Bill Gates's recent companywide memo exposed his fears that his "nightmares" about rivals were coming true. Walt Disney Co.'s Jeffrey Katzenberg waxed eloquent for 28 pages on the need for cutting costs.

Maybe it's the terror they induce in employees. Maybe it's just the power of entertaining prose. But hop-to-it memos, whether distributed, leaked, or purloined, are joining power ties and low golf handicaps in the executive arsenal. Who knows? You too may soon feel a need to reach out and shake somebody via memo. If so, take a few lessons from the masters:

■ **It doesn't have to be a memo to be a memo.** Akers' now-infamous remarks about people standing around water coolers and the sorry state of IBM's work ethic was actually a transcript from informal spoken comments. The rapscallion transcriber even passed along Akers' profanity. But there's a moral: Should word get around that your company has become staid, mouth off in the vicinity of a good note-taker. It'll become a memo soon enough.

■ **Gush it up.** In January, Walt Disney Studios Chairman Jeffrey Katzenberg had Hollywood abuzz with his epic on

what's wrong with the movie biz. Obsessed with selling tickets for big-budget extravaganzas, Katzenberg wrote in passionate tones, the studio should instead "concentrate on what happens in the big room where the lights dim and the magic is supposed to happen."

■ **Invoke other memo-writers.** In his May memo to Microsoft employees, Bill Gates cited as inspiration what he termed a "brilliantly written and incredibly insightful" memo from the founder of Autodesk Inc. in Sausalito, Calif.

He even offered to make copies available. The president of Bridgestone/Firestone Inc. noted in an employee publication that he shares "Mr. Akers' frustrations."

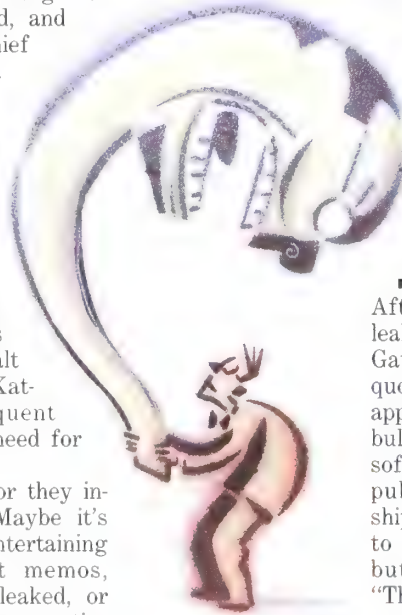
■ **Expect leaks, but always act as if your memo were top secret.**

After a series of techno leaks, excerpts from the Gates memo were widely quoted, and the full text appeared on one electronic bulletin board. But Microsoft remains stalwart. Its public-relations agency ships copies of the memo to "selected reporters" but with this caveat: "Though in providing it to you we realize you may

quote from it... we ask that you treat the document confidentially and that you not circulate the memo widely among your staff or to anyone outside [your publication]."

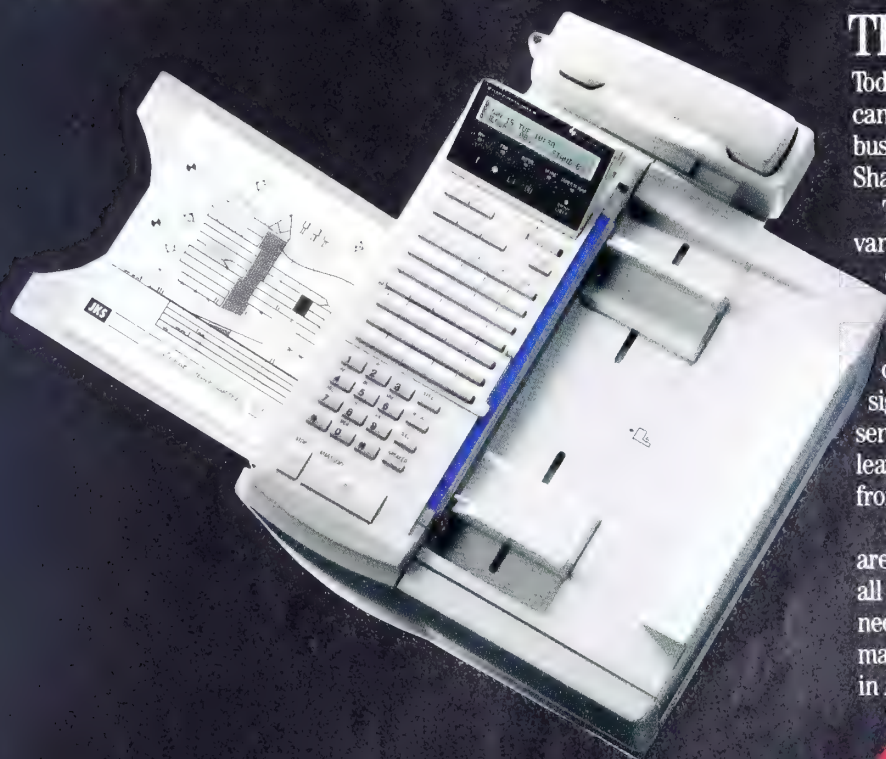
■ **Brace for the parody backlash.** At biotech firm Genentech Inc., a stern memo on drug testing once prompted a counter-memo urging employees to deposit a urine sample on the desk of a certain vice-president. Katzenberg's memo prompted a well-publicized parody urging Disney staffers to take a "voluntary" 88% pay cut, the refusal of which would entail no adverse consequences "other than losing their jobs." Sophomoric? Inevitably. But guess what? Employees like to blow off steam, too.

By *Joan O'C. Hamilton* in San Francisco, with bureau reports



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EDITED BY HARRIS COLLINGWOOD

THE CROWDED SKIES OVER PAN AM

► Pan Am's final chapter is getting interesting. Delta, United, and Chicago investor Jay Pritzker are all still in the running. Delta offered slightly more than \$200 million for Pan Am's remaining European routes, its Frankfurt hub, and its Northeast-corridor shuttle, says one creditor. But that bid will face pressure. United—which is bidding for Pan Am's Latin American system—also wants the routes to France, the transatlantic routes out of Miami, and some of the Airbus jets Delta has asked for. Pritzker, meanwhile, is still looking to take over the whole airline.

Off on the sidelines, one of Pan Am's major creditors has also taken the offensive. Several sources confirm that federal Pension Benefit Guaranty is arranging a bid for the Pan Am Shuttle. Because of missed pension payments, the PBGC has a \$53 million lien on the shuttle's equity. So it has wooed fellow creditor General Electric Credit and a European buyout company called Overseas Partners to construct an offer.

A bid would be a long shot at best. But by floating its own shuttle deal, the PBGC might also pressure Delta. Pan Am has an unfunded pension liability of \$840 million. The more Delta pays, the more the pension agency will get. Whatever happens will have to happen quickly: Sources say Pan Am is fast running out of cash.

swindler Ivan Boesky. Mulheren was sentenced to one year in jail and ordered to pay \$1.7 million in fines.

In reversing the convictions, the appeals court slammed the government's evidence. It also raised serious doubts about the prosecution's theory that Mulheren allegedly helped Boesky manipulate the price of Gulf & Western stock. The reversal is another setback for former U.S. Attorney Rudolph Giuliani, who in recent weeks has watched the appeals courts overturn many of his prosecutorial victories.

SIX STATES JOIN THE OUTCRY OVER TRW

► Acting on consumer complaints, six states have filed suit against TRW, one of the largest providers of credit reports, which affect nearly every American's ability to borrow. The suits, representing New York, Texas, California, Michigan, Idaho, and Alabama, charge the Cleveland-based credit-reporting agency with misleading consumers, disregarding their privacy, and failing to assure the accuracy of reports. TRW insists that its practices are legal, and it has already requested that the suits be thrown out. The company is also fighting a \$290,000 federal court award granted to a Wyoming consumer who claims that TRW deliberately put errors in his credit report.

The legal fireworks are a

HOW'S THE MONTEREY DOING, JACK?

Commodities trading: The phrase conjures up bellowing traders, lightning-fast price moves, market capitalism at its most frantic. Well, usually, but not at perhaps the least-known such market in the country, the National Cheese Exchange in Green Bay, Wis. The 20 or so cheeseheads, uh, traders, who meet there every Friday swap cheddar and set wholesale prices for the big cheeses—Kraft, Beatrice, Borden, and others.

That's a lot of clout. But the Cheese Exchange can't match the hurly-burly of other commodities pits. The traders drift in throughout the morning, chat a bit, then scratch prices on a chalkboard. "It's a lot like watching paint dry," remarks Edward Jesse, an agricultural economist from the University of Wisconsin, who has witnessed the so-called action. And when traders complain that prices stink—they've dropped by about 25% so far this year—they're not far from the truth.



blow to the credit-reporting industry, which is under fire from consumer groups. Congress, meanwhile, is preparing legislation to strengthen and update the 20-year-old Fair Credit Reporting Act.

DIRECT-DIAL IS COMING TO MOSCOW

► For some travelers to Moscow, the frustration of waiting hours for international calls will soon come to an end. On July 10, GTE announced plans to provide a phone network in Moscow hotels and business centers to allow individuals to make and receive direct-dial calls.

GTE has entered into a joint venture with the Soviet Com-

munications Ministry to build and operate telephone and fax services linking Moscow to North America, western Europe, and Asia. GTE will put up most of the \$5 million to \$10 million initial capital investment. The wireless service, scheduled to start in November, will use microwave links to satellites.

NORDSTROM'S UNION FACES A RECALL VOTE

► Nordstrom's fight against its union may be entering its final phase. On July 17 and 18, employees in five Seattle-area Nordstrom department stores will decide whether to decertify their union, Local 1001 of the United Food & Commercial Workers. That's the union that barraged Nordstrom with negative publicity and lawsuits last year. Its main charge: that the Seattle-based retailer was violating hourly wage laws by forcing employees to work unpaid overtime to attend company meetings, stock shelves, and provide extra services such as home delivery to customers.

Both sides are campaigning heavily. But Nordstrom, with greater access to employees, seems headed for a big win in the decertification vote.

ANOTHER GIULIANI WIN GETS THROWN OUT

► Wall Street got a measure of revenge on July 10, when the U.S. Court of Appeals in New York reversed the conviction of arbitrageur John Mulheren. Last fall, he was convicted of securities and wire fraud, largely on the testimony of confessed stock



DEWAR'S PROFILE:

MARK SALZMAN

HOME: Los Angeles, California.

AGE: 29.

PROFESSION: Author, actor, martial artist. "I know everyone in L.A. says that, but really, I am."

HOBBY: Going to the zoo. "It's the one place I won't be asked about China—except by, maybe, the pandas."

LAST BOOK READ: *Discos and Democracies China in the Throes of Reform*, Orville Schell.

LATEST ACCOMPLISHMENT: Writing the script and starring in the movie "Iron and Silk," based on

his book about his experiences as an English teacher in China.

WHY I DO WHAT I DO: "What else do you do with a degree from Yale in Chinese Language and Literature?"

QUOTE: 之呼者也

PROFILE: Animated, ebullient and prone to colorful exaggeration.

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THE SELLING OF CLARENCE THOMAS

William H. Rehnquist had them. So did Henry Kissinger. Robert Bork had them, though it didn't do any good. And now that Supreme Court nominee Clarence Thomas is about to undergo trial by fire in the Senate, he is following a great Washington tradition: putting his fate in the hands of skilled lobbyists who will try to disarm his fiercest opposition.

They're called "minesweepers," and the White House has one of the savviest handling Thomas. As the 43-year-old federal appeals court judge makes the rounds on Capitol Hill, he's being guided by superlobbyists Kenneth M. Duberstein and C. Korologos, Republican veteran who managed the confirmation of Justice David H. Souter last year.

The style of the two couldn't be more different. Korologos is a feisty minnow of the Nixon White House. Principal in Timmons & Co., a top corporate lobbying outfit, he is well versed in Senate politics. The less combative Duberstein, a former Chief of Staff for President Reagan, is well connected with GOP moderates.

ORDER TRIAL. While Korologos works the Hill collecting votes, Duberstein will try to choreograph the confirmation. In carefully controlled public appearances, Thomas will be told to stress his hard-battle upbringing in the segregated South. He'll play down opposition to affirmative action and will express gratitude to the civil rights movement for making his success possible. Thomas faces a grueling summer preparing for his September confirmation hearings. Senators revel in the challenge of finding a candidate into mistakes. Thomas' coaches plan a back hearing, known as a "murder board," in which they hit the nominee as hard as they can. "We pretend we're senators and ask the most foul and rotten things," says Korologos. All the coaching in the world won't make Thomas' confirma-

tion a romp. Although he has yet to state a position on abortion, suspicious feminists have already declared their opposition. Because the question of a constitutional guarantee of abortion rights will soon come before the Supreme Court, Thomas may be able to evade the issue. But he'll have to be more forthright on whether a constitutional right to privacy exists—the basis for the high court's 1973 abortion decision.

The nominee's other challenge is to prevent civil rights groups, which are disturbed by his opposition to racial preferences, from uniting against him. The strategy is to keep the NAACP, the most important group, out of the fight. President

Bush is personally lobbying NAACP Executive Director Benjamin L. Hooks and won a crucial round on July 8, when the NAACP deferred taking a position. "If the civil rights lobby does a job on Thomas, that could destroy him," says a Thomas adviser.

Even great coaching won't work if a candidate can't take advice. Bork's script called for him to convince the Senate that he was a genial moderate, but he wouldn't go along. The Administration expects no such freelancing from Thomas, who survived difficult confirmations to become chairman of the Equal Employment

Opportunity Commission and a judge. "Clarence is a very smart guy," says a senior Administration official. "He's been through this before."

Still, nothing can really prepare someone for the intense scrutiny a Supreme Court nominee gets. That's why the judge will be grateful to have Duberstein and Korologos by his side. And what's in it for the handlers? National recognition, the gratitude of the President—and moving to the top of the Rolodex the next time a harried CEO wants to hire someone to get his company out of a jam in Washington.

By Tim Smart and Douglas A. Harbrecht



CONFERRING WITH SENATE GOP LEADER ROBERT DOLE

CAPITAL WRAPUP

INTELLIGENCE

The Bush Administration may find itself relying on the kindness of a democrat to salvage the nomination of Robert M. Gates as director of the Central Intelligence Agency. Gates's confirmation, which once seemed a sure thing, was thrown into doubt on July 9, when former CIA official Alan D. Fiers pleaded guilty to lying to Congress about the intelligence agency's role in the Iran-*contra* scandal. Fiers' plea has revived suspicions on the Senate Intelligence Committee that Gates, the No. 2 official at the CIA when funds were secretly diverted to the *contras*, knows far more about the affair than

he has been willing to admit. But Intelligence Chairman David L. Boren (D-Okla.) remains a staunch supporter of Gates and could pull him through.

TAXES

Senator Lloyd Bentsen (D-Tex.) may prove a friend in need to the crippled real estate industry. Bentsen, who has long looked after developers' interests, is seeking a way to give investors some tax incentives. Among the possibilities: encouraging pension funds to invest in commercial mortgages and easing restrictions on the deductibility of real estate losses. The big problem remains finding a way to pay for any new breaks.

MEDICARE

Computerized matchups of medicare, Social Security, and tax records could end up saving the government \$1 billion. The Health Care Financing Administration has asked 800,000 employers to provide details on the health coverage of specific individuals to find out if their claims were mistakenly paid by the government. For workers over age 65, medicare pays only for those medical expenses not covered by employer-provided insurance. An HCFA study of the computer-generated data, however, found that medicare shelled out hundreds of millions of dollars that should have been covered by private insurers.



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THE FRIENDS OF CARLOS SALINAS

The President encourages rich cronies to buy state companies—and toughen up their own

One starry night, Mexican television magnate Emilio Azcárraga Milmo was lounging on the deck of his yacht, bobbing at anchor in the Pacific. Looking up at the sky, he noticed a wandering speck of light. Told it was probably an errant satellite, Azcárraga immediately got on the phone to business associates in Mexico City, inquiring about the value of lost satellites. By the end of the evening, Azcárraga had spun out a rudimentary business plan for yet another ambitious company, a satellite-retrieval service.

The idea soon fizzled. But Azcárraga, one of Mexico's super-rich, is used to losses. His incursion into U.S. journalism, for example, went belly-up when his sports daily, *The National*, closed down in June, costing Azcárraga a cool \$100 million. Until recently, it didn't matter much. Azcárraga's grip on a virtual private television monopoly in Mexico, Televisa, provided a seemingly endless flow of cash. That's the way Mexico has operated for years: The country's closed market has been a private fishing pond for a select handful of families with strong political connections.

But times are changing for Azcárraga and the rest of Mexico's powerful business plutocracy. Mexico's decision to enter a North American free-trade agreement with the U.S. and Canada promises an unprecedented wave of competition. Now, Mexico's cosseted power elite will have to take on the likes of Anheuser-Busch, Du Pont, 3M, and Turner Broadcasting, which are poised to flood the Mexican market with everything from Bud Light to Headline News.

HARD-PRESSED. As rich as they may be, members of Mexico's business elite will be hard-pressed to summon the capital and expertise they need to ward off the Americans. Mexico's largest snack-food company, family-owned Gamesa, for example, has already sold out to PepsiCo Inc. "This is just the beginning," says Lorenzo H. Zambrano, chief executive of Cementos Mexicanos, North America's biggest cement maker.

But tough shakeouts aren't all bad in the eyes of Mexican President Carlos



Salinas de Gortari, the chief architect of the free-trade strategy. He recognizes that Mexico's economic system needs to be rejuvenated and modernized after decades of relative isolation. His goal is to use free-trade to encourage Mexico's power brokers to recast the structure of Mexican business. Of course, Salinas wants to do this on Mexico's terms, with top Mexican industrialists serving as partners for powerful foreign players. Thus, the often painful steps that Mexico's top industrial families are now taking will determine how well the country responds to a Yanqui invasion—and how

open Mexico will be to the outside world.

Salinas is clearly not out to destroy Mexico's power elite—he's part of it. The son of a onetime presidential hopeful, he rode horses and studied with the scions of the country's richest families. Many of them live in lavish, high-walled estates in the hilly Lomas neighborhoods high above the smog-blanketed city.

To prepare for free trade, Salinas is asking his childhood friends to play a major role by buying up big chunks of state-run companies—from commercial banks to steel mills. This ensures that management remains in Mexican hands

draws back billions in Mexican capital flight. But to supplement their foreign stashes, Mexico's elite must also pluck capital markets in New York and London, seeking new and imaginative financing. Salinas also wants them to pare back their high-margin conglomerates



His horse-riding Salinas friend is carving out niches in auto parts and plastics. Now he's after Banamex, the No. 1 bank



His '80s buying spree gave him control of a slew of companies from copper to tobacco. Now he's also after Banamex



The billionaire broker missed on attempted buyouts of the phone company and Telcel. But he seems due for a bank

to smaller entities better able to handle tough competition from the North. Reflecting the enormous power of the Mexican presidency, Salinas is, in effect, picking who wins and who loses in the new Mexico. But he faces risks. By turning to his cronies, Salinas isn't doing

much to diversify corporate control. If free trade sours the Mexican economy, Salinas stands to take the blame. Leftist critics are already blasting him for handing the nation's treasures to the super-rich. Historian Lorenzo Meyer of the Colegio de México compares Mexico's industrialists to their American counterparts of a century ago. "They're like the old robber barons in the U.S.," he says. "Connections are everything."

But Salinas recognizes that for Mexico's winners, the rewards can be enormous: a foothold in the \$5.5 trillion North American economy. One such winner is Carlos Slim, 51, a portly Mexican-Lebanese financier who made a fortune



■ This baron of North America's biggest cement maker is better placed than other magnates. But he needs big money fast



■ Televisa Chairman Azcarraga made millions selling cheap TV programming. Can that work under free trade?

riding the Mexican stock market in the 1980s. Then, last December, he cornered a gold mine, landing a controlling share of the phone monopoly Teléfonos de Mexico. The \$3.9 billion company earned a stunning \$1.1 billion last year.

Most of this summer's privatization-jostling is in finance. The government is selling the entire commercial-banking system. The big prize is Mexico's No. 1 bank, Banamex. Bids are already in for the bank, whose market capitalization of \$3.95 billion places it halfway between Chase Manhattan Corp. and Citicorp. Whoever wins control will emerge as a titan in North American finance.

The two leading candidates come from new and old money. From the old aristocracy: Fernando Senderos Mestre, 41, and his brother-in-law, Carlos Gómez y Gómez. On his 18th birthday, Senderos received an early inheritance of several hundred million dollars from his father, Manuel, the former owner of Telmex. Unlike other "juniors" in Mexico, the young Senderos didn't throw his money around. But he did make one extravagant purchase: a prize-winning, U.S.-bred horse, Jet Run. The horse paid off in other ways: Senderos' friend and teammate on the Mexican squad was a young rider named Carlos Salinas de Gortari.

VENEER OF IMPARTIALITY. Lined up against the Senderos team is Roberto Hernandez, 49, the epitome of Mexican new money. "Ten years ago," jokes one Senderos friend, "Roberto Hernandez couldn't even finance his American Express card." That changed in a hurry. During the 1980s, as principal owner of the brokerage firm Acciones y Valores, Hernandez rode Mexico's booming stock market to billions in profits. That gave him the base to bid for control of the phone company, which he lost to a group headed by Slim, Southwestern Bell, and France Telecom. Now, he thinks he has a good chance at the September sell-off of Banamex.

Such maneuvering is putting an uncomfortable spotlight on Salinas. Rumors and allegations of cronyism swirl around the privatization process. In response, the government goes to great lengths to create a sense of impartiality. At the Cabinet meeting to determine the new owners of Telmex, for example, the three bidders were listed as A, B, and C. But everyone knew which was which. "We're not selling oranges here," says one Cabinet secretary.

To blunt political attacks and win support for the privatizations, Salinas has limited foreigners to minority shares in most companies. What's more, in an attempt to fragment capital, he has established a 10% limit for personal holdings in banks. Both of these limits play well in the nationalist wing of his party. But in fact, they favor the super-rich. First of all, foreigners are limited to minority stakes within any Mexican investment group's bank holding. And by limiting individuals to 10% stakes in a bank, the government allows the rich to secure control without having to buy 51%, freeing up millions for other investments.

Consider how the government sliced up the giant telephone company into controlling and noncontrolling shares. That permitted Slim, head of Grupo Carso, to buy effective control with only 5% of its shares—an outlay of some \$400 million. Joining him in the controlling block are Southwestern Bell and France Telecom,

JAPAN

along with investors from Mexico's old-rich families. The government later sold the remaining shares in the Mexican market and in a \$2 billion equity offering in foreign stock markets.

As Mexico's rich brace themselves for the North American free market, many will have little choice but to take private companies public. Take Azcárraga's Televisa. Few Mexican companies better illustrate the traditional tit-for-tat relations between the government and big business. Televisa has enjoyed a near-monopoly for decades, thanks in part to its staunchly pro-government politics. During the 1988 presidential campaign, Televisa's coverage flattered the ruling Institutional Revolutionary Party even more than its state-owned competitor. That pro-government line protected Televisa and discouraged the government from opening the door to competition.

NOVEL PREDICAMENT. But now that the government is selling its own nationwide network and negotiating the free-trade pact, Televisa's monopoly days are numbered. And Azcárraga finds himself in a novel predicament: He needs cash. The plan is to take Televisa public, selling 15% of the company for \$300 million to investors in Mexico and abroad.

The restructuring trend has also reached Monterrey. After 100 years of dominating Mexico's steel, glass, beer, cement, and plastics markets, the web of families that holds up Monterrey's empires is undergoing a transformation. When Lorenzo Zambrano, an engineering graduate of Stanford University, saw free trade coming, he knew his family-owned Cementos Mexicanos could compete with only one product: cement. So he unloaded Cemex's petrochemical business, and two years ago, he went far into debt to buy Cementos Tolteca as well as affiliates throughout the U.S. Southwest. That made Cemex the largest cement maker in North America—and well-positioned to take on Yanqui competitors.

Others among Mexico's super-rich stand on shakier ground. If the Americans prevail in the free-trade talks, tearing down investment and finance restrictions, hordes of Americans and Canadians—and perhaps Japanese and Europeans—could storm the fiefdoms of Mexico's elite. In that case, chortles Zambrano, "they'll still be rich, but they won't be powerful anymore."

Don't count on it. The betting is that Salinas will succeed in attracting foreign capital while keeping the country's jewels, from the banks to its precious oil company, in Mexican hands. Salinas, a shrewd calculator, knows better than to put his powerful friends out of business.

By Stephen Baker in Mexico City

RYUTARO HASHIMOTO: JAPAN'S MR. TOUGH GUY?

His career depends on cleaning up the securities scandal quickly



FINANCE MINISTER HASHIMOTO: A LIKELY SUCCESSOR TO KAIFU

Rarely has Japan seen such a spectacle. On July 9, the Finance Minister Ryutaro Hashimoto, with tears glistening in his eyes, publicly accepted responsibility for Japan's dangerously widening stock market scandal. The powerful minister announced that he and two senior aides would punish themselves by taking 10% pay cuts for three months.

Concerned about his and Japan's reputation, Hashimoto is racing to put a lid on the scandal. He would like to have it under control before he and Prime Minister Toshiki Kaifu arrive in London for the Western industrial summit on July 14. A quick end to the crisis is essential to restoring investors' confidence in Tokyo's shaken market (chart). Beyond that, if Hashimoto can't contain the damage, his position as a leading candidate to succeed Kaifu in the fall could be badly crimped.

Hashimoto has moved boldly so far, cracking down on Nomura Securities Co. and three other brokers at the heart of the scandal. Calling their behaviour "shameless," he ordered all four to cease trading with corporate clients for four business days. The brokers also were hit with penalties and back taxes for improperly deducting \$870 million in payoffs. Following the ministry's cues, several cities as well as government agencies are boycotting them. "The point is to make sure the problem does not happen again," says Hashimoto.

There's no sign yet that the financial turmoil is abating. Several of Japan's trust banks are thought to have followed the brokers' practice and covered losses for favored customers. In another shocker, tax authorities say Tadao Yo-



Uchida, president of zipper maker YKK and one of Japan's leading philanthropists, understated his income by about 100 million. As such revelations of misdeeds continue to pile up, Hashimoto's opponents question whether he has enough control over his ministry's powerful bureaucrats to force any real change in Japan's insular markets. More bad news, analysts warn, could knock the market down an additional 2,000 points or more after its 40% plunge since 1989.

Backing up Hashimoto's tough talk, the Finance Ministry is mulling stiffened regulation of brokers and the market. But many experts doubt that there will be any follow-through. "There's limited manpower, so perfect regulation is difficult," says Teruiki Uchida, deputy director of the ministry's Securities Bureau. "It's not necessary to have an SEC in Japan." As long as that attitude prevails, investors will probably remain skeptical.

INDEPENDENT POSE. The scandal could weaken Hashimoto in the ruling Liberal Democratic Party. A tough debater in a world where compromise is prized, Hashimoto has alienated some LDP luminaries during his 27 years in parliament. He isn't enough of a backslapper," says one member of his faction. Rumors are now spreading that Hashimoto's political rivals will try to oust him from the ministry after the Group of Seven summit. While few think such an attempt would succeed, new, unpleasant surprises could make Hashimoto vulnerable.

Hashimoto's take-charge attitude has earned him additional points with the Japanese public. Even before the stock market mess, polls showed him as the most likely candidate to succeed Kaifu. And in Japanese popularity polls, women voters find his youthful good looks appealing.

Since taking over the Finance Ministry in the wake of another scandal two years ago, Hashimoto, 53, has struck an unusually independent pose. Last summer, he brushed aside protests from the budget bureau and boosted Japan's infrastructure spending to \$3.1 trillion in response to U.S. requests.

Overseas, Hashimoto has quickly gained a reputation for being a tough bargainer in the two years since his appointment. He is perceived as pushing Japan's interests more forcefully than his predecessors ever did. "Hashimoto is clearly of the younger generation, and he brings a different approach to problems," says a Bush Administration official. "He has seen the strong rebirth of Japan, while the older leaders knew the reconstruction days and Japan's dependence on the U.S."

But the stock market scandal may lead Hashimoto into a new fight with

While embarrassing, the penalties imposed so far have been little more than a light slap on the wrist

Washington. U.S. trade officials are already pointing to the Tokyo brokers' favoritism to longtime clients as the latest evidence of the barriers faced by Americans in Japan. Hashimoto is likely to respond stoically that Japan can hardly be accused of foot-dragging on cleaning up the mess. In addition to being censured by the Finance Ministry and fined by the Tokyo Stock Exchange, the "Big Four" brokers—Nomura, Daiwa, Nikko, and Yamaichi—have cleaned house themselves.

But while such moves have proved

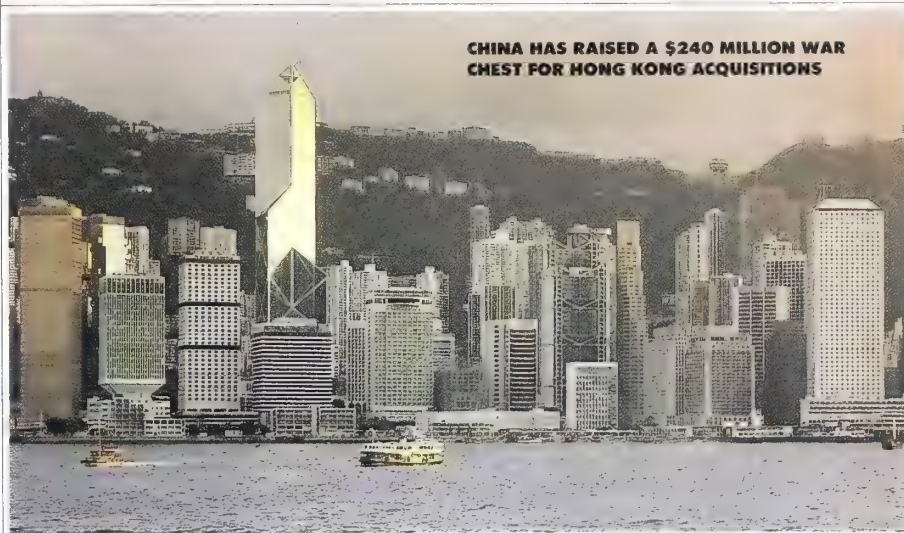
embarrassing, the penalties imposed so far are little more than a light slap on the wrist. Indeed, while the ministry's 136-person Securities Bureau is too understaffed to monitor the country's 267 brokers, Hashimoto has rejected recent calls from business leaders to set up an independent body similar to the Securities & Exchange Commission.

Meanwhile, the once vibrant Tokyo Stock Exchange is in a blue funk. Nervous underwriters recently persuaded camera maker Nikon Corp. to drop an issue of warrants, and Japanese life insurers are urging other corporate issuers to halve their plans to raise \$7 billion a month in new equity this summer.

It looks like Hashimoto will have to bang more heads before he can credibly claim Japan's markets are clean. Doing that without capsizing the stock market will require all his political skill.

By Ted Holden in Tokyo, with Amy Borrus in Washington

HONG KONG



CHINA HAS RAISED A \$240 MILLION WAR CHEST FOR HONG KONG ACQUISITIONS

IT'S ONLY 1991, BUT IT ALREADY FEELS LIKE 1997

A \$10 billion airport deal makes it clear that China calls the shots

A wave of euphoria swept through Hong Kong's business world on July 4. That was when a beaming Sir David C. Wilson, the colony's governor, told Hong Kong's assembled press corps that China had dropped its objections to a much-debated \$10 billion airport project. The Hang Sang stock index responded by shooting up to a near-record high. "This is a ray of sunshine," said Howard Gorges, a director of South China Brokerage Co., over the din of the firm's frantic trading room.

You would have hardly known that the big winner in the airport pact was

Hong Kong's future landlord. China never denied that a replacement for congested Kai Tak airport was a must. Instead, it used the difficult negotiations to gain more influence over the current management of the colony. Not only did the Chinese authorities secure a seat on the enclave's airport authority, but they also won a strong voice in the planning and awarding of contracts for \$16 billion in future projects, ranging from a new subway line to the world's longest suspension bridge. China had feared that British authorities might be gearing up a last-minute construction boom to strip

BRITAIN

the enclave's treasury of its estimated \$9.4 billion in cash before Hong Kong comes under mainland control in 1997.

Critics, such as liberal Hong Kong legislator Martin Lee, were quick to assail the new pact as another British sell-out of the enclave's autonomy. But to most citizens, it was a grudging admission of the obvious. Although full transfer of authority is six years away, China is rapidly gaining influence over Hong Kong's affairs. Without China's endorsement, for instance, banks were not willing to pony up for the airport project.

BIG STAKES. As the countdown to 1997 proceeds, China has been quietly increasing its clout by purchasing big stakes in many of the colony's leading businesses. In the past two years alone, Beijing-controlled companies bought their way onto the boards of Dragon Airlines Ltd., Hongkong Telecommunications Ltd., and Asia Satellite Telecommunications Co. China International Trust & Investment Corp. (CITIC), China's primary foreign-investment vehicle, recently announced that it has raised a \$240 million war chest from private investors. So, additional acquisitions are likely.

The mainland's growing economic presence has raised surprisingly little protest. The business community says China will hesitate to crimp the enclave's freewheeling capitalism if it has a stake in the action. Hong Kong companies are also betting that by sidling up to China, they will be better able to protect their interests after 1997. By selling 12.5% of Cathay Pacific to CITIC in 1985, Britain's Swire family eased fears that China would transfer critical landing rights to a mainland carrier. Says Hongkong & Shanghai Banking Corp. economist Alan McLean: "There can be a distinct commercial advantage in having China on your team."

Hong Kong executives say that so far, their Chinese investors are keeping politics out of business. But not everyone is confident that China will exercise similar restraint in the future. Lee, leader of the United Democrats of Hong Kong party, calls the airport pact "a dangerous precedent that poses a very severe threat to the future autonomy of Hong Kong"—which China promised in 1984, when it secured the eventual right to control of the colony. Lee also fears that party cadres will now demand influence over franchises for everything from bus service to utilities, as well as control over Hong Kong's courts and media licenses.

But many executives argue that no law will prevent China from cracking down on Hong Kong if it feels like it. So, why not try to co-opt the cadres into capitalism before 1997?

By Peter Fernandez in Hong Kong

NELSON PELTZ HAD A PERFECTLY DREADFUL TIME IN LONDON, THANKS

The U.S. dealmaker heads home, leaving Mountleigh \$1.1 billion in debt

As U.S. leveraged buyouts began to wilt in late 1989, dealmakers Nelson Peltz and Peter May thought they saw fresh pickings in Europe. So they took \$150 million of their takeover haul and parlayed it into control of Mountleigh Group PLC. It looked like a perfect investment vehicle.

Their plan for Mountleigh, an erratically performing London-based property developer, echoed the tactics in the U.S. during the go-go 1980s.

They wanted to unload real estate and to turn Mountleigh into a takeover machine. But the high-powered duo quickly found that their new-world style clashed with London's conservative financial community. And their high-stakes strategy was ill-timed for Britain's sharp recession.

Now, Peltz is moving back to the U.S., abandoning his acquisition goals in Europe in favor of what he calls the "more familiar" market at home. "We see more opportunities in the U.S.," says Peltz, who will spend most of his time with his New York investment company, Triam Group LP, a \$1 billion collection of industrial and real estate operations. Peter May never moved to Britain.

Mountleigh is struggling with \$1.1 billion in debt and a share price of 42¢, 87% less than when Peltz and May bought. The extent of Mountleigh's problems was unveiled in early July when it announced that property write-offs had contributed to a \$155 million pretax loss for fiscal 1991 and forced the company to renegotiate bank credit lines for the second time in a year.

GLITZKRIEG. At Mountleigh, the golden touch Peltz had shown for making huge profits from prosaic U.S. companies turned to lead. With the help of Michael Milken's junk bonds, Peltz turned New York-based Triangle Industries Inc. into

the world's largest can maker. He then sold it to France's Pechiney and others for \$1.3 billion.

But Peltz's London foray was less fortunate. Peltz's glitzy lifestyle was fodder for the rough-and-tumble British media. And Peltz took his stake in Mountleigh just as the British real estate market was about to crash and as banks were pulling in their horns on takeover financing. Property sell-offs

went far slower than anticipated, and as a developer, Mountleigh operations generated little income.

Still, Peltz hunted for European deals. With developer Elliott Bernerd, he looked at buying British retailer Sears PLC, owner of Selfridges Ltd., the landmark London department store. In February, he surprised investors by shifting his buying interest to the U.S., where he attempted an exceedingly complicated takeover of Fairchild Corp., an industrial conglomerate. "Nelson tried very hard," says Jeffrey Steiner, chairman of Fairchild and a longtime friend. "But the bankers in England don't have the same way of doing business Drexel did."

In the meantime, Clive Strowger, a respected former finance chief at conglomerate Grand Metropolitan PLC, will try to revive Mountleigh. Now CEO at Mountleigh, he hopes to unload real estate worth \$648 million within two years. He is also counting on fresh equity from such heavyweights as Chicago's Pritzker family and a trust controlled by oil scion Gordon P. Getty.

As he heads back home, Peltz is still hungry for deals. But he'll find that the U.S. is now gripped with the sort of old-world stodginess found in London. That could crimp his style.

By Richard A. Melcher in London



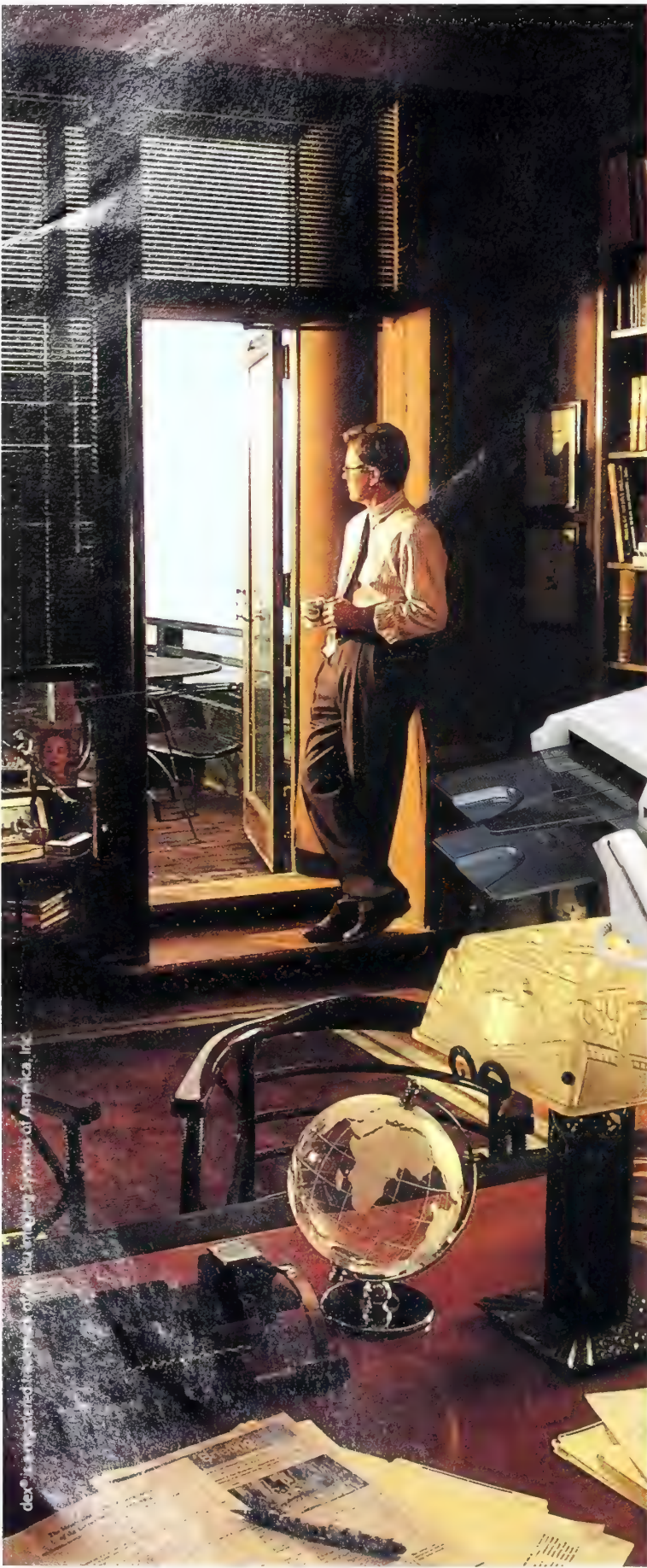
BAD TIMING: PELTZ'S GO-GO TACTICS FLOPPED IN THE BRITISH ECONOMY'S SHARP GO-SLOW



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HOW MANDELA CAN STILL LEAN ON THE SANCTIONS LEVER

Nelson Mandela, the symbol of the anti-apartheid movement, was subdued. Even as the African National Congress on July 7 concluded its first national conference in South Africa in 30 years with a striking display of unity, the ANC's newly elected president couldn't help but mourn the imminent passing of the international sanctions effort against Pretoria. "We want to continue to hold the line on sanctions," he admonished more than 2,000 delegates. "But unless there is a great deal of flexibility and imagination, we shall be left holding a shell and nothing else."

That shell may prove more durable than Mandela is letting on. As President Bush lifted all sanctions against South Africa on July 10, the ANC was set to launch a strategy to discourage state and local governments in the U.S. from doing the same. The result: These state and local anti-apartheid laws are likely to become a new lever in Mandela's drive to negotiate a transfer of political power to South Africa's black majority. If he succeeds, he will prevent a mass movement of U.S. business into South Africa any time soon.

TRUMP CARD? It's not as though the ANC can stop the anti-sanctions bandwagon. With Washington's easing of restrictions on investment and trade, Denmark remains the only holdout in the European Community. President F.W. de Klerk's progressive moves to dismantle apartheid have opened a flood of new commercial contacts with formerly hostile African and Eastern European countries, as well.

But by keeping the sanctions issue in the public eye, Mandela is hoping to make the most of a wasting asset and exert some control over the pace of South Africa's reintegration into the global economy. The ANC plan is to phase out sanctions gradually as Pretoria takes steps toward democratic rule. The ANC is prepared to support the lifting of sanctions on South

Africa's international sports participation, cultural exchanges, and travel restrictions when political prisoners are released and when the government helps end widespread violence. The lifting of sanctions on trade, foreign investment, and financial ties is linked to the establishment of an interim government to manage the transition to democratic rule. Only with the formation of a democratically elected government will the ANC call for an end to arms and oil sanctions.



ANC PRESIDENT MANDELA AND HIS WIFE, WINNIE

In the U.S., ANC lobbyists will be active from Capitol Hill to city hall. The Congressional Black Caucus, which opposed Bush's decision to lift sanctions, wants to preserve a congressional ban on International Monetary Fund loans to South Africa. Locally, anti-apartheid activists will work to keep laws penalizing businesses that deal with South Africa. Says Daniel O'Flaherty, vice-president of the National Foreign Trade Council: "Those companies that have to choose between state or local contracts in the U.S. or the market in South Africa will still be in a dilemma."

Opponents of sanctions aren't likely to get much support, either. Even Bush is treading lightly: He will soft-pedal his termination of sanctions to avoid alienating black voters. As a goodwill gesture, he plans to double U.S. aid to South Africa's poor, to \$80 million a year. The White House is even sending business subtle hints to go slowly when it comes to investment in South Africa. Companies also see little gain in pressing for an end to local sanctions. "All of the people who would otherwise like to see the sanctions lifted won't get out in front," says Michael Clough, an Africa specialist at the Council on Foreign Relations. Given these hesitations, Mandela is likely to find that U.S. sanctions are still a powerful political weapon.

By Bill Javetski in Washington, with Alan Fine in Johannesburg

GLOBAL WRAPUP

JAPAN

Did Treasury Secretary Nicholas F. Brady get his numbers wrong? For months, he has badgered the Japanese to cough up a final \$700 million he says they promised for the gulf war. But now, he may find the Japanese actually overpaid. Reliable Washington sources have told BUSINESS WEEK that internal Defense Dept. estimates of the war costs are coming in on the low side—and that Defense is padding the costs. "No way you can make that war cost more than \$40 billion," says Lawrence J. Korb, a former Assistant Defense Secretary now at the Brookings Institution. The Pentagon is stick-

ing to its initial estimate: \$61 billion.

If the reports are true, they're sure to cause more furor in Japan, where raising a hefty \$9 billion for the war ignited a political fire storm. "There may be a point where we pay back money," says one U.S. source. Germany, which shelled out \$6.5 billion, may also press for a refund. German Finance Minister Theodor Waigel says if the final tally is low, "we'll certainly talk about it."

CUBA

When the Presidents of 20 Latin American countries gather in Guadalajara, Mexico, on July 16 to commemorate the 500th anniversary of

Columbus' voyage, one leader will stand out as particularly desperate: Cuba's Fidel Castro. As his Soviet patrons retrench, Castro must seek financial salvation from his Latin American neighbors. But they'll exact a price. After all, they don't want to be pitted against the gringos just when they're all seeking free-trade deals with the U.S. While on stage, the leaders will give speeches on how Christopher Columbus got them where they are today and will pay homage to Spain's King Juan Carlos and Portugal's President Mário Soares. Behind the scenes, they'll lobby the increasingly isolated Cuban to cut out his inflammatory rhetoric and liberalize his regime.

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TEXACO: FROM TAKEOVER BAIT TO DYNAMO

How James Kinnear has not just saved his company—he has made it an innovative force

James Kinnear, 52, is a man of many talents. A former Marine, he served in Vietnam and was wounded in action. After returning home, he worked for the U.S. Navy and then for the U.S. Coast Guard. In 1984, he joined Texaco as vice president of operations. In 1987, he became president and chief executive officer. In 1988, he was elected chairman of the board.

When James Kinnear joined Texaco in 1984, the company was in a state of crisis. It had lost its way, and its stock price had fallen to a low of \$10 a share. Kinnear's first task was to stabilize the company. He did this by focusing on the company's core business—oil exploration and production—and by cutting costs. By 1987, the company's stock price had risen to \$25 a share.

Kinnear's message was clear: Texaco was not just a company that sold oil. It was a company that explored for oil. And he made this message clear by focusing on the company's core business—oil exploration and production—and by cutting costs.

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CRASH MAKEOVER. In 1987, Texaco's stock price had fallen to a low of \$10 a share. Kinnear's first task was to stabilize the company. He did this by focusing on the company's core business—oil exploration and production—and by cutting costs. By 1987, the company's stock price had risen to \$25 a share.

share in net worth, prompting raider Carl C. Icahn to mount a takeover and proxy battle that year.

Four years, a bankruptcy, and a takeover fight later, Kinnear has pulled off one of the most startling comebacks in U.S. corporate history. The crisis atmosphere of October 1987, the opportunity to refashion the company in ways he might never have managed in more normal times. Kinnear has shed \$7 billion in assets and 10,965 employees. And he has reshaped virtually all of the company's operations, from the way it manages its exploration in Sumatra to the way it sells high-test

—Harvard

In the process, Kinnear has transformed a rigid, oil-poor company into a focused, innovative, and growing force in the industry. Says onetime nemesis Icahn, who publicly skewered Kinnear and Texaco during his takeover challenge: "Since the proxy fight, I wish to hell I'd kept the stock."

Icahn has reasons for regret. Texaco has not its cost of capital of equity at 15% to 30% today. Its cost to find a barrel of oil has plunged from more than \$9 in 1985 to \$3.88 in 1990 (charts, page 52). And with the help of the oil price run-up prior to the Persian Gulf war, earnings have soared from \$861 million, before asset sales, in 1989 to \$1.4 billion on \$41.9 billion in revenues in 1990. Even though oil prices have edged downward 37% from their wartime heights, the new Texaco is positioned for a nice earnings ride. Paul D. Miotok, an analyst at Morgan Stanley & Co., figures Texaco's profit growth will cruise at an average of 14 a year through 1995, compared with 11% for other major integrated oil companies.

tory enjoyed by Pennzoil and Chairman J. Hugh Liedtke hasn't been a panacea. Battered by fierce competition, sagging natural-gas prices, and a troubled diversification effort, Pennzoil's earnings have recently fallen off (page 53).

Texaco's stunning reversal of fortune has surprised even its own directors. Says Thomas S. Murphy, Texaco director and chairman of Capital Cities/ABC Inc.: "If you had told me a few years ago that we would be in the shape we are now, I simply wouldn't have believed it." Icahn's former nemesis still hasn't added much oomph to its stock, though. At about 60, it's up only some 4% since the start of the year.

OIL DRAIN. Investors have reason to be wary. While Texaco was struggling to survive, Exxon and Royal Dutch/Shell Group were plowing money into technologies such as computer-generated seismic imaging that could lead to the next big oil find. And Texaco needs a gusher. Despite its successes, Texaco has one of the shortest reserve lives—the number of years its current reserves would last—among the majors. Until recently, Texaco actually used up more of its oil reserves than it replaced through acquisitions and exploration. In short, it was burning its reserves at a alarming rate, while rivals were slogging around the planet finding new oil fields.

Kinnear has now made exploration a bigger priority at Texaco. Late last year, he announced a \$21 billion capital spending plan for Texaco's exploration and refining operations. The program nearly doubles annual spending to \$3.1 billion in 1991, from \$1.5 billion back in 1988. Already, his efforts have placed Texaco on a more equal footing with global rivals. Texaco ranked No. 2, behind Atlantic Richfield Co., in a Wertheim Schroder & Co. analysis reviewing the production and exploration track records of the majors since 1986, based on such factors as production costs and reinvestment rates.

Texaco is still heavily reliant on foreign oil, though. Back in 1988, Saudi Arabia and Texaco set up Star Enterprise, a joint venture to which the Saudis



IN THE TAKEOVER
BATTLE, KINNAR
SHOWED THE PUBLIC
RELATIONS SAVVY
HIS PREDECESSORS
LACKED



quired a half-interest in Texaco's refineries and gas stations in 23 states—a direct pipeline into the world's largest energy market. In return, Texaco got access to an ocean of oil. There's a big downside, however. About 60% of Texaco's refined product sales could be vulnerable if Saudi production is disrupted. The man who has transformed Texaco's culture spent his entire working life steeped in it. He joined Texaco's marketing department in 1954, after the U.S. Naval Academy and duty in Korea. In those days, Texaco relished its reputation as an industry maverick. "The company had a kind of militaristic culture, and you had a series of CEOs who ran it that way," says one former Texaco executive. It was also notoriously arrogant.

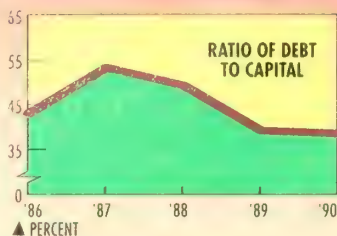
One big reason: Texaco was one of the few oil companies that grew up independently from the mighty Standard Oil trust, whose 1911 breakup spawned such rivals as Exxon, Mobil, and Amoco. **FEW SURPRISES.** Kinnear, however, has rarely let Texaco's rigid ways cramp his style. At 31, he was sent to Hawaii to build Texaco's retail operations on the islands from scratch. There, he slashed gasoline prices to match those of competitors. In three years, he had grabbed 8% of the market—quite a feat in such a fragmented business. "I've been on the competitive kick since," he says. Kinnear's star really started to rise, though, when he took over as president of Houston-based Texaco USA in 1982. Kinnear turned things around at the

marketing and refining arm, closing or selling inefficient refineries and spending \$2 billion to revamp more promising ones. He also cut Texaco's money-losing U.S. retail network in half, to 2,500. The result: While the Texaco USA unit lost an average of \$200 million annually from 1981 to 1984, by 1985 the unit had turned a \$10 million profit. The next year, it posted a \$145 million gain. Few were surprised, then, when Texaco's chairman at the time, John K. McKinley, elevated Kinnear to vice-chairman in 1983. Kinnear stayed in Houston, and that turned out to be a blessing. McKinley and Texaco President Alfred C. DeCrane Jr., Kinnear's chief rival for the top job, orchestrated the Getty deal from the company's White Plains (N. Y.)

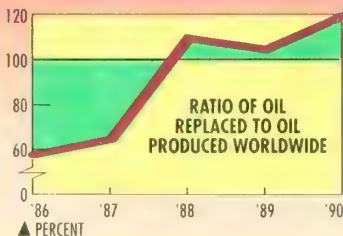
TEXACO'S RISING STAR

DATA: COMPANY REPORTS
JOHN S. HEROLD INC.

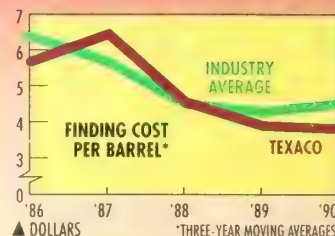
IT'S PAYING DOWN DEBT...



...FINDING MORE OIL...



...AND DOING IT MUCH MORE EFFICIENTLY



headquarters. They also took a real shel-lacking for the debacle. When Texaco's board gathered in late 1986 to name a new chief, Kinnear was the obvious choice. His vast operational experience gave him an edge. So did his popularity among employees—a sharp contrast to the old regime, for whom “the only difference between a person and a pump was that the pump is depreciable,” says a union official. The board gave Kinnear the CEO job and day-to-day management responsibility, while DeCrane assumed the role of chairman.

SLUMPING STOCK. Then all hell broke loose. In April, 1987, the U.S. Supreme Court refused to shield Texaco from a lower-court ruling that required an \$11 billion bond. Crude-oil suppliers soon suspended deliveries, and bankers began to demand more security. On Apr. 12, Texaco Inc. and its two subsidiaries—Texaco Capital N.V. and Texaco Capital Inc.—filed for Chapter 11 bankruptcy protection.

With Texaco's stock trading at depressed levels, Icahn soon acquired a 14% stake and eventually offered to buy the rest of the company for \$12.4 billion. Kinnear refused, and Icahn launched a proxy fight to oust the CEO and seat himself, together with four others, on Texaco's board.

Kinnear struck back with the public-relations savvy that his predecessors had always lacked. He and DeCrane made a whirlwind cross-country tour, pressing the flesh with pension-fund and insurance executives. Kinnear also attacked Icahn as a quick-buck artist in newspaper ads. In the end, Kinnear prevailed, but not before Icahn garnered 41% of the vote. “I thought the assets would have been better off in someone else's hands,” says one institutional holder who voted with Icahn. “I would have made a big mistake.”

The scare forced Kinnear to rethink the whole company. He needed to restructure Texaco. And he had to raise \$3 billion, the sum finally agreed upon by Texaco and Pennzoil to settle the Getty affair. What followed was one of the

largest sell-offs in corporate history—and the emergence of a leaner and more profitable Texaco. In June, 1988, Kinnear sold Deutsche Texaco, a German subsidiary, for \$1.2 billion. It still wasn't enough. So Kinnear also sold off one of the company's most cherished assets: Texaco Canada Inc. That turned out to be a shrewd move. The \$2.04 billion unit was generating only \$120 million in cash flow, thanks to tax complications involving the repatriation of earnings. Texaco sold the unit to Imperial Oil Ltd. of Canada for \$4.15 billion, netting \$3.24 billion for its 78% stake.

Kinnear also shook up Texaco's bureaucracy, putting his popularity to the

market share—including sales by Star Enterprise—hit 6.5%, up roughly a quarter of a percentage point from 1989, while total volume rose 3.1%, according to Lundberg Survey Inc. Another edge: Texaco is a leading producer of methyl tertiary-butyl ether, a key ingredient used in the reformulated gasolines required by the Clean Air Act.

Kinnear's biggest coup though, has been to recast Texaco's exploration process. Before, each division came up with its own exploration plan. With each team hoping to strike a gusher, that often caused an imbalance of high- and low-risk wells. Texaco's replacement rate lurched up and down. Now, managers are schooled in a portfolio strategy balancing sure-fire projects and long-shot efforts.

A BIG PAYOFF. Kinnear has also given more freedom to his exploration staff, which once had to wait months for executives to sign off on new wells. One payoff: In December, 1989, Texaco learned of a discovery in a Malaysian field. A manager rushed through a process that used to take up to two weeks and quickly had a bid in hand for the property. Within a day, he was on a plane headed for Kuala Lumpur. Texaco now owns a partial interest in the site and plans to start drilling on Aug. 1.

Texaco has come a long way—but there's more to be done. Its reserve life of about 8.8 years lags behind Exxon's 11.3 years and Amoco Corp.'s 11.7. Texaco also needs more in-house technological savvy. Royal Dutch/Shell and Exxon have spent billions on computer-aided exploration that can deliver color-coded topological models and pinpoint remote oil and gas wells. Rivals say that Texaco has to hire out some of the reading of this data. Sniffs one competitor: “We'd never hire out interpretation.”

Kinnear acknowledges that he still has work to do. But remember that Texaco once had a rather tight noose around its neck. For Kinnear and Texaco, it's been quite a reprieve.

By Todd Vogel in White Plains, N.Y., with Brian Bremner in New York



HIGH TIMES IN '85: PENNZOIL LAWYER JOSEPH JAMAIL AND LIEDTKE

test. He instituted a tough program that pegged salaries to performance at the divisions. He also broke with Texaco's insular tradition of promoting only from within. “We wanted some new blood,” Kinnear says. So, he lured away Allen J. Krowe, a former executive vice-president at IBM, to serve as Texaco's CFO. In all, six top Texaco officials would come from outside the company.

Through all Texaco's travails, Kinnear refused to scrimp on research and development. Texaco pumped \$15 million into one product, called System³. The aim: to create an engine-cleaning, high-performance gasoline. System³ is now the brand name for virtually all of Texaco's gasoline offerings. Since its launch in 1989, Texaco's sales have picked up momentum: In 1990, the company's total

PENNZOIL'S TRIP DOWN A SLIPPERY SLOPE

Oil tycoon J. Hugh Liedtke isn't one to be trifled with. Back in 1965, Pennzoil Co.'s chairman expertly executed a hostile raid on United Gas Corp., a large gas pipeline operator, remaking his company into a major player in the oil patch. Consider, too, that when Texaco Inc. snatched Getty Petroleum Corp. from Pennzoil's clutches in 1984, Liedtke instinctively went for the jugular. He slapped Texaco with a \$15 billion lawsuit, charging with illegally usurping Pennzoil's pending merger deal with Getty. In the end, Texaco declared bankruptcy and worked over a \$3 billion settlement to Pennzoil. Talk about sweet revenge.

Or was it? The windfall has proven something of a curse for Pennzoil. In late 1989, Liedtke invested nearly \$2 billion of his booty to acquire an 8.8% stake in Chevron Corp.—and has since raked in about a \$400 million gain on paper. But fearing a takeover run from the acquisitive Liedtke, Chevron sued Pennzoil for allegedly violating securities laws by misrepresenting its stake as a passive investment, sparking a nasty legal row.

LUCK. And how's this for a twist: While Texaco has rebounded, Pennzoil has sputtered along. Its energy earnings, after a two-year recovery, are falling again. And its market-leading motor-oil unit hasn't picked up the slack, nor have recent acquisitions helped. There's even talk Pennzoil may restructure. "No one expected it to be

like this," says a former executive.

Liedtke's bad luck started almost as soon as he cashed Texaco's check. In 1988, Pennzoil acquired Facet Enterprises, a maker of car and industrial filters—later renamed Purolator Products Co. after its best-known brand—for \$350 million. However, the unit has been battered by a price-cutting campaign from foreign suppliers. After pumping in some \$50 million to shore up operations, Pennzoil last year took an \$82 million write-down to reflect the unit's lesser value. Now, Pennzoil would be lucky to fetch \$200 million for it, figures Salomon Brothers Inc.

Pennzoil's core energy businesses have misfired, too. Since 1986, its worldwide replacement costs have averaged \$7.70 a barrel, second-highest among the U.S. majors, according to industry research firm John S. Herold. Worse, half of Pennzoil's energy reserves are in natural gas, a market stung by a string of mild winters and plummeting prices. All this explains why Salomon Brothers figures Pennzoil's earnings will fall 12%, to \$83 million, this year, on \$2.1 billion in sales.

True, Pennzoil's motor-oil products

business still boasts a market-leading 22% share. Yet it faces stiff competition from Quaker State Corp. and others that are flooding discount chains such as K mart Corp. with motor oil. Major oil companies are discounting, too. Especially—guess who? "Texaco," groans a former executive. "They're killing everybody."

Last March, Liedtke replaced his CEO of two years, Randal B. McDonald, with James L. Pate, Pennzoil's treasurer. The new chief has shaken up management, trimmed Pennzoil's work force by 7%, and squeezed out annual savings of \$25 million from overhead.

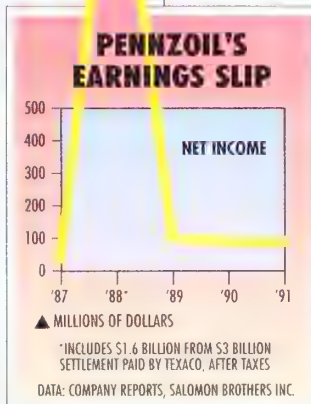
TAX-FREE? That helps, but Pennzoil still faces a possible tax time

bomb. Back in 1989, Liedtke hoped to shield Pennzoil from \$800 million in potential taxes on the Texaco settlement. How? The company argued that the award represented an involuntary conversion of assets—Getty Oil—that it would not have made had it not been for Texaco's meddling. By investing the proceeds in another oil company, Pennzoil wanted to get off tax-free. The Internal Revenue Service has yet to decide how much, if anything, Pennzoil should pay. The company could face a tax bill of up to \$675 million, plus \$125 million in interest.

Things are coming to a head with Chevron's lawsuit, as well. The action was summarily tossed out of Federal District Court in San Francisco last year, and an appeal pending in the Ninth Circuit Court is a long shot. Once the dispute is resolved, speculation is sure to mount regarding a restructuring of Pennzoil, whose stock is trading around 74. That's well below the estimated \$83-a-share breakup value, reckons Salomon Brothers.

What's in store? Liedtke isn't saying, but odds are he will sell Pennzoil's refining and marketing arms or its sulfur-mining operations. Or he could spin off the Chevron stake, now 9.4%, into a separate trust. Any way you shake it, some sort of makeover seems certain. If so, it will be an ironic turn for a company that once seemed so turbocharged—and so ready to roll.

By Mark Ivey in Houston



PENNZOIL'S MARKET-LEADING MOTOR OIL IS FEELING THE HEAT FROM PRICE-CUTTING RIVALS

THE LONG AND WINDING ROAD TO BCCI'S DEAD END

It took painstaking effort for global cops to shut the shady bank down. Could they have been quicker?

It has been fined for laundering drug money in Florida and embroiled in a foreign-exchange scandal in Kenya. Its clients have included former Panamanian strongman Manuel Noriega and Colombian drug lords. It may have violated U.S. law by using front men to acquire a Washington (D.C.) bank. You name it, and the Bank of Credit & Commerce International probably has been accused of doing it. Yet for almost 20 years, BCCI nearly always managed to stay ahead of the law.

No longer. In an unprecedented international operation on July 5, regulators from the U.S., Britain, and five other countries swooped down on local BCCI offices, shuttering most of the sprawling, \$20 billion bank for good. The reason: A report commissioned by the Bank of England from BCCI's auditors, Price Waterhouse, disclosing massive bad loans, unrecorded deposits, blatantly phony accounting, and other offenses. "There was firm evidence," says John B. Atkinson, the Cayman Islands' inspector of banks and a member of the international team that shut BCCI down. "It was fraud."

Losses from BCCI could exceed \$5 billion, making it one of the world's biggest banking failures. The brunt of the losses will be borne by thousands of depositors, mostly in Europe, the Mideast, and Asia. But the single biggest loser is likely to be Zayed bin Sultan al-Nahayan, Abu Dhabi's ruler, who invested \$1 billion in BCCI stock only last year in hopes of turning it around.

With Abu Dhabi now controlling 77% of the bank's shares, international regulators are now pressuring al-Nahayan into making good on at least some of BCCI's commitments. Before the crack-down, the ruler had been planning to

inject several billion dollars more into the bank as part of a sweeping restructuring. High-ranking investigators believe al-Nahayan wasn't fully aware of the wreckage behind BCCI's facade.

In the wake of the sudden shutdown, depositors, banking experts, and politicians around the world are raising tough questions. Given BCCI's shady reputation, why didn't regulators spot and deal

legislation requiring the home countries of foreign banks to strictly supervise offshore subsidiaries. Says Michael A. Mackenzie, Canada's Superintendent of Financial Institutions: "I recommend saying: 'You can't operate in my country until we're satisfied that your home-country regulation is capable of doing the job.'" With police in Britain, a U.S. Senate subcommittee, and grand juries

in Washington, New York, and Miami now probing BCCI's affairs, more intensive scrutiny of all banks operating across borders seems nearly certain.

It was the absence of a global regulatory approach that let BCCI thrive (table). Founded in 1972 by Pakistani financier Agha Hasan Abedi, it seemed designed from the start to evade banking oversight. BCCI's registered home base was Luxembourg, but its managers were based in London. Its shareholders were rich Persian Gulf oil sheiks, and its assets were scattered in a branch network that encompassed more than 70 countries.

To further complicate matters, many operations were channeled through the Caymans. That "didn't permit any banking authority to conduct normal regulatory activities," says Nicholas Schaus, director of the Monetary Institute of Luxembourg. BCCI's tight-knit staff didn't make regulators' jobs any easier. Says Roger F.G. Alford, a London School of Economics banking expert: "Massive wrongdoing, where everybody colludes and every single figure is a fake, is much more difficult to spot."

In 1987, regulators became sufficiently concerned about the lack of information on BCCI that Luxembourg, Britain, France, Spain, Switzerland, and the Caymans formed a special "college" just to



IN LONDON: "MASSIVE WRONGDOING... EVERY SINGLE FIGURE IS A FAKE"

with its problems earlier? What responsibility, if any, should be borne by Price Waterhouse? Price, BCCI's sole auditor since 1987, failed to provide any explicit public warnings about the bank's health until the fateful report to the Bank of England. And most important, how can a repeat of BCCI be avoided?

TIGHTER GRIP. The final question may be the toughest one of all. Even before the BCCI scandal broke, concerns about global money-laundering had spurred many industrialized nations to consider tighter controls on international banks. The Federal Reserve, for instance, has proposed

are notes. But the college didn't include many countries in which BCCI had operations, including the U.S. And even when BCCI's problems became public, regulators remained unwilling to go beyond their own borders. "Everyone was looking at the pieces, and no one was looking at the entity," says Federal Reserve Governor David W. Mullins Jr. In 1988, for example, a Senate subcommittee took sworn testimony from a former BCCI manager that the bank had handled illicit money from Noriega and might capital throughout South America. But the testimony had little impact. "Did the regulators look at it closely enough?" asks London banking analyst Robin Conro-Davies. "Intuition tells you they didn't."

Under the loose regulatory net, Abedi constructed what, for a time, appeared to be a successful global business. Concentrating on trade finance and retail accounts, the bank's mostly Pakistani managers built an enviable network of branches in the Mideast and Third World at a time when most Western banks were pulling back from these areas. Even in the most obscure reaches, BCCI "knew everybody," marvels Mustapha Sereldin, London-based head of the Bank of Kuwait in the Middle East. **CASH CACHE.** But one Mideast banker says BCCI succeeded, in part, because it did "whatever it took to get the job done." Among other things, BCCI won a reputation for helping heavily indebted Third World countries hide cash

from international monetary authorities by shuffling deposits among branches. BCCI had an international reputation for capital flight, tax fraud, and money laundering," Manhattan District Attorney Robert M. Morgenthau recently told a Senate committee.

The biggest blow to BCCI's standing—and its business—came in 1988, when a federal sting operation led to the indictments of the bank and 10 executives in Florida on charges of laundering drug money. The bank pleaded guilty and was fined \$15 million, and five of the executives were also found guilty and jailed.

The trial threw up a raft of questionable BCCI ties to accused international drug traffickers. It was also a red flag to regulators, who started to look more closely at BCCI. "If it hadn't been for the undercover sting, the other nefarious activities the bank was engaged in might never have come to light," says Charles Intrigato, publisher of the Miami-based newsletter *Money Laundering Alert*.

BCCI's problems started snowballing after that. Prosecutor Morgenthau launched a probe last summer of possi-

BCCI loans that were never repaid. Clifford denies any wrongdoing.

The growing legal dragnet exacerbated BCCI's mounting financial problems. It lost at least \$150 million trading Treasury options between 1984 and 1986, and was obliged to obtain an infusion of capital from the family owners of the National Commercial Bank of Saudi Arabia, who then owned 22% of BCCI. Then, as bad news mounted and clients fled, BCCI ran up a \$498 million loss in 1989.

Fed up, the Saudis sold their stake for

\$600 million to Abu Dhabi's al-Nahayan, who injected an additional \$400 million in capital and promised to restructure the bank. Around the same time, founder Abedi, who had undergone a heart transplant in 1988, resigned as president.

The Abu Dhabi connection helped calm European banking authorities, who assumed the emirate would stand behind the bank. But by this time, BCCI was apparently resorting to extreme measures to deal with its deteriorating finances. One ex-manager says an internal audit given to the bank's board early in 1990 alleged widespread abuses. Then, earlier this year, a BCCI officer tipped the Bank of England about widespread finagling. "They used all imaginable means to make up false accounts," says Luxembourg regulator Schaus.

The central bank's revelations come as small comfort for the thousands of small savers who may have lost their life savings in a bank they thought was

safe. In many of the Third World countries where BCCI operated, deposit insurance is nonexistent. Even in Britain, where BCCI had 120,000 accounts, depositors are insured for only \$24,000. In the future, these and other depositors are likely to be more wary of a friendly banker's pitch. And maybe when the next rogue bank appears, regulators who permitted BCCI to get out of control will ask tough questions a lot sooner.

By Mark Maremont in London, with Blanca Riemer in Paris, Gail DeGeorge in Miami, Suzanne Woolley in New York, and Catherine Yang in Washington

A HIGH-FLIER'S RISE AND FALL



AGHA HASAN ABEDI

1972 Pakistani financier Agha Hasan Abedi sets up Bank of Credit & Commerce International in Luxembourg with backing from Bank of America, Arab investors

1978 Abedi and ex-Carter Administration aide Bert Lance unsuccessfully try to buy Washington's First General Bankshares

1980 Complaining it lacked access to BCCI's books, Bank of America sells stake

1981 Arab investors linked to Abedi and BCCI buy First General, rename it First American Bankshares. Former Defense Secretary Clark Clifford named chairman, says bank is independent of BCCI

1985 Bank loses at least \$150 million in Treasury options market

1988 Ten BCCI executives charged in Florida with laundering \$32 million in drug money. Investigators disclose BCCI ties to former Panamanian strongman Manuel Noriega. Accused executive tells federal agents BCCI secretly controls First American

1990 BCCI reveals \$498 million loss for 1989 and pleads guilty to money laundering. Abedi resigns as president, and Zayed al-Nahayan, Abu Dhabi ruler and longtime shareholder, invests \$1 billion and takes control

1991 Grand juries in New York, Washington, Miami probe BCCI. Federal Reserve orders BCCI to sell First American shares. Unidentified BCCI official warns Bank of England of illegal transactions, and Price Waterhouse ordered to investigate. After Price finds widespread fraud, Britain, U.S., and other countries seize most BCCI assets and close branches

DATA BW



ZAYED AL-NAHAYAN

ble money-laundering links to BCCI's New York branch, which spurred Washington regulators to take a closer look. Early this year, the Federal Reserve concluded that the 1982 takeover of First American Bankshares Inc. by Mideast investors with BCCI ties had improperly given the bank control of the Washington holding company.

EXIT THE SAUDIS. Clark M. Clifford, First American's chairman and Washington superlawyer, had maintained to regulators that his bank was independent of BCCI. But he and other investors in First American stock bought the shares with



MAKING THE ROUNDS: McNAMEE'S HIGH-TECH FUND AT T. ROWE PRICE ISN'T FOR THE SQUEAMISH

PORTRAIT OF THE TECHIE AS A FUND MANAGER

For Roger McNamee, nothing works like shoe-leather research

Roger B. McNamee prowls New York's cavernous Jacob K. Javits Convention Center, where PC Expo, a computer trade show, draws hundreds of exhibitors and thousands of visitors. Like many, he's weighed down with a bag of promotional literature. But he isn't shopping for notebook-size computers, laser printers, or Windows software. Instead, McNamee, who runs the top-rated T. Rowe Price Science & Technology Fund Inc., is carefully watching the shoppers.

"Look at WordPerfect," he says, pointing to the crowd gathered for a demonstration. "And some in the industry say that program is dead." He takes a pass at Santa Cruz Operation, which sells UNIX software for PCs. "That's the third time today I've gone by, and there's still no one there. If people were unhappy with Windows, they'd be looking at UNIX." He stops at NCR Corp. to see its new notebook computer that's operated by a pen rather than a keyboard. "Pen-based computing," he proclaims, "is the next wave."

McNamee also engages exhibitors in conversation, asking for demonstrations of their products and for opinions of others. "Roger's outgoing and charismatic, and people open up to him," says Bill

Grubb, president of The Complete PC Inc., a privately held company that makes computer peripherals. "He gets more information than most analysts."

And most of that information is grist for McNamee's approach to high-tech investing. He's trying to identify important trends and the companies with products that will capitalize on them. The 35-year-old fund manager doesn't worry

about forecasting quarter-to-quarter earnings. If you're right on the product cycles, he says, the profits will follow.

McNamee attends about 15 trade shows a year. Throw in industry meetings, brokerage-firm conferences, and on-site visits to companies, both public and private, and McNamee logs about 140 days a year on the road. Three associates also spend much time out of the office. "The mission is to penetrate the industry and develop a network of contacts similar to that of an industry executive or consultant," he says. "It's 'participative' research."

FIVE STARS. Whatever it's called, it works. Since he took over the portfolio in September, 1988, the Science & Technology Fund, through June 30, has delivered a total return of 74% vs. 50% for the Standard & Poor's 500-stock index. More important, Morningstar Inc., which takes risk into account, gives the fund five stars—the only one of 18 technology funds to earn the top grade. As of June 30, the fund had assets of \$143 million.

Make no mistake: This fund is not for the squeamish. In the first quarter, it was sensational—up 43%, the best technology fund and fourth best of all equity mutual funds. In the second quarter, when many tech stocks were mauled, the fund lost 12% of its net asset value. It was the second-worst technology fund and the fifth-worst of all funds.

"Am I disappointed?" asks McNamee. "Yes. Am I surprised? No." Big swings, he says, go with the territory, and it has happened before. Without the 28% cash cushion he built after the first quarter runup, the fund might have fared even worse. Still, for the first half of 1991, the fund gained 25.5% vs. a 17.8% average for technology funds.

"Roger has strong convictions and takes big positions in companies he believes in," says Edward J. Mathias, a managing director at T. Rowe Price. "And he also admits his mistakes quickly." One such wrong turn was Compaq Computer Corp. After two tumbles this spring that took the price from the low 70s to about 50, McNamee loaded up on the stock. "Those sell-offs were usually good buying opportunities," he says. "I thought the second shoe had dropped."

Then, within days, the company dropped another bomb, and the stock plunged 20%. He sold out. Says McNamee: "Compaq had three shoes." In retrospect, the portfolio manager violated one of his own rules. "The stock was cheap, but the new-product pipeline was dry," he says. "And product cycles are what drives high-tech earnings."

Still, dismal second-quarter results haven't changed McNamee's plans. The trends for industry growth are still the

McNAMEE'S TOP TEN HOLDINGS

Company	Percent of fund assets
ADOBE SYSTEMS	7.0%
APPLE COMPUTER	6.0
CIRRUS LOGIC	4.0
PHOENIX TECHNOLOGIES	3.5
MICROSOFT	3.0
NOVELL	3.0
DELL COMPUTER	3.0
SUN MICROSYSTEMS	3.0
INTERGRAPH	2.5
REUTERS HOLDINGS	2.5

DATA: T. ROWE PRICE SCIENCE & TECHNOLOGY FUND

me. One is "portability"—smaller, lighter, more powerful PCs. "Desktops are a mature business," he says. "Everyone who wants one has one." Networking groups of PCs together is another growth area. A third is the graphical user interface (GUI), systems such as Microsoft Corp.'s Windows that let a user point to a symbol on a screen instead of typing computer commands. For McNamee to invest heavily in a company, it must be operating in one or more of those fields. Adobe Systems Inc. is the major provider of software for electronic printing and publishing. He

He really gets excited about technology. He's not just waiting for something better'

ays it fits the GUI theme. Apple Computer Inc. hits GUI, networking, and, late this year, portability, too. Novell Inc. is the premier provider of networking software. Cirrus Logic Inc. and Phoenix Technologies Ltd. both work in portability and GUI. Phoenix, which the fund started buying last year at \$3, provides software that makes different PCs compatible. The stock, now at 8½, is one of the few to escape getting clobbered during the second quarter.

OF LEVITY. Although he can carry on about bits and bytes, McNamee is not a schweenie. In fact, he's a lively speaker who injects a little levity to make his points about the perils of his trade. "Science fiction," he explains, "is the stuff between covers of the prospectus for an initial public offering." Says Helen Johnson, who follows technology funds for Morningstar: "He really gets excited about technology. He's not just waiting for something better to come along."

McNamee graduated with a history degree from Yale University in 1980 and earned an MBA from Dartmouth College's Amos Tuck School in 1982. He went to T. Rowe Price as a research analyst—first in aerospace, then telecommunications, and later office products. In 1986, McNamee switched over to the fast-changing technology beat. "It's my personality," he says. "High energy level, short attention span."

With technology stocks beaten up, is it the time to buy? Indeed, as the stocks tumbled, McNamee spent most of his cash adding to positions and establishing new ones, such as Dell Computer Corp. and AST Research Inc. Although the fund is up more than 5% since July, McNamee could be setting himself up for a fall. But that's the way he plays. And his record shows he usually wins.

By Jeffrey M. Laderman in New York

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BOSTON CO. LEARNS ALL THAT GLITTERS . . .

Dumping celebrity loans is turning around the AmEx unit

When Donald Trump bought his yacht *The Princess* in 1988, he didn't have to throw a lavish celebration party. His lender threw it for him. Boston Co., the American Express Co. subsidiary that loaned Trump the \$29 million purchase price, spared no expense. Champagne and caviar flowed as top executives toured the 282-foot yacht at its berth in Boston Harbor. For Boston Co. Chairman James N. von GERMEN, the Trump loan represented the transformation of his firm from a stodgy trust-fund manager for New England's old-line elite to a big-time backer of the *nouveaux riches*, especially celebrities and real estate developers.

Trump is now trying to avoid bankruptcy, and Boston Co. has repossessed *The Princess*, although it will be lucky to get \$10 million for it. After much financial distress, the company is beginning to turn its own ship around. And it may be a tough sail. Von GERMEN was fired in 1989 after an internal review revealed that Boston Co. falsely inflated 1988's pretax profits by \$44 million. Von GERMEN declined comment. In 1990, Boston Co.'s main unit reported a \$138 million loss and added \$90 million to its loan-loss reserves. And in the first quarter of 1991, domestic nonperforming loans increased to \$155.9 million from \$39.9 million in 1989 and constitute nearly 20% of its \$343 million personal-loan portfolio.

REVERSE COURSE. All of which has been yet another embarrassment for AmEx and its beleaguered Shearson Lehman Brothers Holdings unit. In good years, Boston Co. contributed 25% of Shearson's bottom line. Yet for the past two years, it has hobbled AmEx's aggressive efforts to turn Shearson around.

In charge of the turnaround effort is former AmEx treasurer John R.

Laird, who was installed as CEO in September, 1989. Laird, 49, is engineering a fundamental strategy shift that is starting to show results. He has scaled back the high-risk personal-banking business and shrunk assets from \$17.4 billion in 1988 to \$9.3 billion. And he is steering Boston into the lower-risk business of providing fee-based financial management services to big institutions, much like crosstown rival State Street Bank & Trust Co. In 1991's first quarter, Boston Co. earned \$21 million, mostly from fee income. "It's moving in the right direction," says John KRIZ, an analyst at Moody's Investors Service. "Its prospects are good."

Indeed, Boston Co. is expected to pro-

vide a boost to Shearson's second-quarter operating profits, although Shearson will post a big loss because of a \$144 million write-off of its stock in First Capital Holdings Corp., the failing California insurer. "Like Shearson, Boston Co. is a turnaround in progress," says Shearson Chairman and CEO Howard L. Clarke Jr.

Laird's first step has been to stop most lending to individuals. "No more celebrity loans," says Laird. The loans had been made by Boston Co.'s main unit, Boston Safe Deposit & Trust Co., a century-old special-purpose bank that can take deposits but only make personal loans. Besides the U.S. nonperforming loans, it has an additional \$61 million in its \$600 million British mortgage portfolio. Yet less than 1% of its \$4.2 billion in jumbo mortgages—\$350,000 or more—is nonperforming. Still, analysts remain skeptical that Boston Co. has solved all its lending problems. "I am still very worried about that loan portfolio," says Alison A. Deans, an analyst at Smith Barney, Harris Upham & Co.

TOO RISKY. Laird's biggest chore has been to liquidate a controversial \$7 billion internal investment portfolio that had been a profitmaker under von GERMEN. Shearson raised the money by selling CDs and then turned it over to Boston Co., which reinvested it in securities. Since 1989, the strategy has yielded only marginal profits. In Laird's view, the risks outweighed the returns.

Laird's big bet is on institutional money management and administrative services. He is increasing institutional assets under management, which grew at double-digit rates for most of the 1980s, reaching \$25.5 billion at the end of the first quarter. Laird expects similar growth from pension fund administration. Boston Co. is the fourth-largest U.S. pension fund custodian, with \$141 billion under administration. While that industry grew only 1.8% last year, Boston Co.'s custodial assets grew 7.7%, according to *Pensions & Investments*, an industry journal.

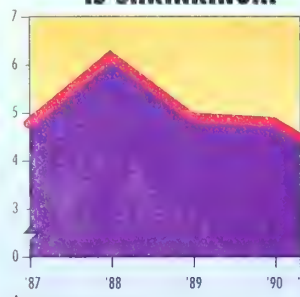
Laird is also looking for a buyer for *The Princess*. If he finds one, that would expunge not only a depreciated asset but a symbol of his company's errant brush with the excess of the Eighties.

By Geoffrey Smith in Boston, with Leah Nathans Spiro in New York

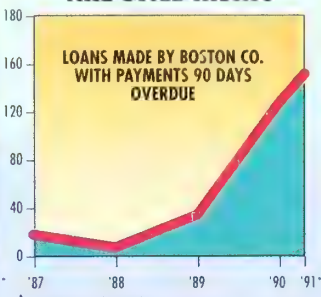
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BY GENE G. MARCIAL

HAS THE STREET MISDIAGNOSED IMMUNEX?

Although Immunex thinks it scored a giant victory in March when the Food & Drug Administration approved the marketing of its first product, GM-CSF, investors didn't quite see it that way. Immunex's stock began to head south—slumping from 59 to 43 on July 9. Some big players worry that the new bio-engineered drug, trademarked as Leukine, won't be able to compete with a widely used Amgen product. But not everyone shares their concern: Investment manager Bill Harnisch has been buying, building up a 12% stake in Immunex recently.

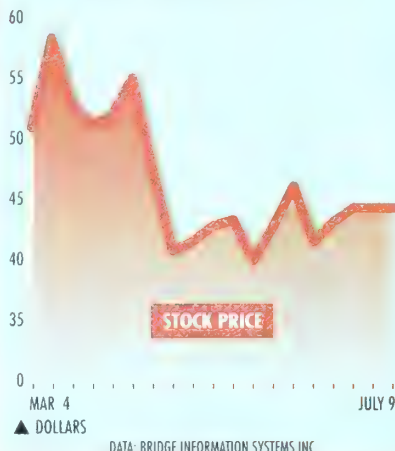
"Immunex's drug is very much misunderstood and belittled by the Street," says Harnisch, the president of Forstmann-Leff Associates. Leukine spurs the growth of infection-fighting white blood cells that are destroyed during cancer therapy, specifically bone-marrow transplants—for which the FDA approved the drug.

Amgen's CSF (colony-stimulating factor) is G-CSF, known as Neupogen, which the FDA approved in February for the broader treatment of infections associated with chemotherapies that suppress white-blood-cell production. Some big investors maintain that Neupogen will knock Leukine out of the market. Not true, says Harnisch, who thinks the CSF market "is much too broad to worry about competition." He figures that it will grow into a \$1.5 billion business over the next five years, with Amgen and Immunex both deriving big profits.

In the red since 1982, Immunex should earn 44¢ a share this year, says Harnisch. As more doctors and hospitals use Leukine in treating cancer patients, he expects profits to jump to \$1 a share next year, reach \$2.10 in 1993, and hit \$5 by 1995.

BROAD CONSENSUS. Stuart Weisbrod, a first vice-president at Merrill Lynch, agrees that Immunex will get more than a toehold in the CSF market. He bases his conclusion on the results of a survey of 4,400 oncologists. His survey shows that both drugs are considered effective by these cancer specialists, with no material difference discerned between the two. And both are being used as adjuncts to chemotherapy and

IMMUNEX: STUCK IN THE DOLDRUMS



bone-marrow transplants, says Weisbrod. He estimates that Amgen will initially garner 75% of the market, with Immunex taking the rest. A third CSF product, developed by Schering-Plough and Sandoz, is expected to be on the market by late 1992. But Weisbrod expects it to have some difficulty cutting into the market shares garnered by Amgen and Immunex.

Peter Drake, an analyst at Vector Securities International, is also bullish on Leukine's prospects and expects Immunex's stock could hit 55 to 60 in the next 12 months.

STEAK HOUSES THAT MAY SOON SIZZLE

The restaurant business has been a major victim of this recession. And, like the rest of the industry, Ryan's Family Steak Houses, which has 131 owned and 34 franchised restaurants, has seen its sales slump and profit margins shrivel. So why have some big pros been eating up the stock in recent weeks?

For one thing, management has been trying to beef up revenues. A recent change that seems to have produced fast results in several of its Florida restaurants is the installation of bakeries that sell fresh breads, pastries, and desserts. The bakeries added 15% to those restaurants' sales, notes one analyst, who believes that Ryan's will introduce bakeries in most, if not all, of its outlets. The company also plans to add 16 restaurants this year.

Aside from being a "nice economic-recovery play," Ryan's is a "perfect takeover stock to start picking up

now," says one New York money manager who has been buying. He puts Ryan's value at \$15 a share—about twice what the stock is selling for.

Never mind that some analysts think Ryan's current price-earnings ratio of 17 is a bit rich, says this money manager. He believes that with the company's clean balance sheet, little debt, and good potential for growth during the coming recovery, "Ryan's is an attractive regional operation for the likes of PepsiCo or Bob Evans Farms." He notes that PepsiCo is beefing up its restaurant business to complement its Taco Bell and Pizza Hut operations. And he adds that Bob Evans, which owns restaurants in the Midwest, is rumored to be in the market for another chain. Most of Ryan's restaurants are in the Southeast. Bob Evans wants to acquire food-related companies, says a spokesperson. PepsiCo says it is expanding its restaurant operations.

SEEING SPARKS AT A CIRCUIT MAKER

Don't be surprised if you haven't heard of HADCO—it's unknown on the Street, too. According to *Nelson's Directory of Investment Research*, only one analyst follows the company. Yet such names as IBM, General Motors, Siemens, and Intel are HADCO customers. Recently, some investors have been buying shares of HADCO, one of the few major independent makers of sophisticated printed circuits. It trades at around 4.

What's sparking the activity? One Boston money manager believes the economic recovery is certain to ignite investor interest in electronics-related stocks. And HADCO, with annual sales of \$160 million, "will be among the quick highfliers once a turn in the electronics business is felt," says the money manager, who has accumulated a 3% stake. HADCO's two-sided, multilayered printed circuits, which connect electronic components, are used in computers, telecommunications, and industrial automation. The computer industry accounts for 60% of sales.

The Boston money manager says earnings are apt to be down in 1991, to 50¢ a share from last year's 65¢. But he expects profits to rebound to 75¢ in 1992 and \$1 in 1993. With lots of cash and little debt, HADCO has been buying back stock—more than 500,000 shares since 1990. Officers own some 42%, including 20% owned by Chairman and CEO Horace H. Irvine II.



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THE SEARCH FOR WAYS TO KEEP AGING PLANES FLYING



It's a worrisome trend: According to the Federal Aviation Administration, the average age of U.S. commercial airplanes is 13 years—and will soar to 20 by the year 2000. Most aircraft have a design life of 20 years. Yet "there is a new damage-tolerant philosophy which says, as long as we increase inspections, we can keep older planes flying long-

" says Chris C. Seher, an FAA expert on aging aircraft. Keeping aging planes aloft will require better methods of spotting metal fatigue and other potential dangers before they lead to catastrophe. Most current procedures, says Seher, are outdated: "80% to 90% of all inspections are done by visual examination using flashlights and magnifying glasses." The FAA plans to change that. This month, the agency will spend \$3.4 million to Sandia National Laboratories in Albuquerque to set up a center to improve nondestructive inspection techniques, such as ultrasound and X-rays, and to probe innovative approaches that might lead to new technologies.

HOW, AN ICEBOX THAT'S COOL FOR THE ENVIRONMENT

How do you make an environmentally friendly refrigerator? The Solar Energy Research Institute (SERI) in Golden, Colo., has developed a new insulating technology, called impact vacuum insulation, or CVI, that should make possible smaller, lighter, more energy-efficient appliances.

CVI panels consist of two thin pieces of tin-plated steel whose edges are hermetically welded together. Constructed in a vacuum chamber or evacuated after manufacture, the panels have an internal array of supports that prevent them from collapsing. A $\frac{1}{10}$ -inch thick CVI panel has the same thermal resistance as a piece of foam insulation more than an inch thick (an R-value of 11). And CVI is not just limited to the kitchen. It can be used in refrigerated trucks, mobile homes, cars, and hot or cold pipelines. Science Applications International Corp. in San Diego has signed a license to develop CVI for commercial use.

ATING THE FIRE HAZARDS IN YOUR LIVING ROOM

Your risk of dying in a fire may soon be much lower, thanks in part to the perseverance of Mark A. Dietenberger, a researcher at the University of Dayton. A half-dozen years ago, he set out to develop a computer program that could predict the potential fire hazard of furniture and other household combustibles. Few researchers thought it could be done, because the dynamics of fire remain largely a mystery. Still, Dietenberger wanted to develop a practical tool that manufacturers could use to gauge fire hazards and develop safer goods. He designed his computer program to use data from a small-scale testing device called the cone calorimeter.

Developed by Vytenis Babrauskas, a researcher at the National Institute of Standards & Technology (NIST), the instrument is the first commercial system that simultaneously measures the parameters of a fire, from heat production and rate of spread to the output of smoke and other gases.

Dietenberger has unveiled the first version of his program, which predicts the fire hazard of different furniture designs and materials. The smoke production calculations need more work, he says. Still, "Mark's program is probably the most complete and competent model yet," says NIST's Babrauskas.

MIRROR, MIRROR ON THE WALL WHOSE COMPUTER IS FASTEST OF ALL?

Although best known for the microprocessors that serve as the brains of IBM-type personal computers, Intel Corp. is also a leader in massively parallel computers. These machines have hundreds of microprocessors and quickly solve complex problems using each processor for a piece of the puzzle.

Intel and archrival Thinking Machines Corp. in Cambridge, Mass., are now fighting over bragging rights for the fastest massively parallel computer. In June, Intel boasted that its newest supercomputer, the Touchstone Delta System installed at the California Institute of Technology, had topped the world speed record set a few months earlier by Thinking Machines. Outfitted with 528 of Intel's two-year-old i860 reduced instruction-set computing (RISC) processors, the Delta breezed through 8.6 gigaflops, or billions of floating-point operations per second. A week later, Thinking Machines edged back on top, claiming 9.03 gigaflops for its CM-200 machine.

That same day, Intel unveiled a souped-up RISC chip, the i860 XP. It will be the heart of a new class of massively parallel supers called Touchstone Sigma. Intel expects to demonstrate that technology late this year and projects a peak speed of 150 gigaflops. In the meantime, the Caltech machine has reclaimed the lead at 11.9 gigaflops.

THIS POISON COULD BECOME A POTENT POTION AGAINST CANCER

Selenium can be a deadly poison, yet researchers know that tiny amounts of the non-metallic element are essential in our diet. Now, they're finding that it may play a role in fighting cancer.

Researchers at the University of Wisconsin at Madison and the Roswell Park Memorial Institute in Buffalo, N.Y., have discovered a selenium

compound that sharply reduces the incidence of breast cancer in rats, without causing any ill effects. Scientists believe the compounds fight cancer by scavenging strong oxidizing molecules that can damage cells.

Whether selenium is toxic or beneficial depends on its chemical form. Inorganic selenium proved to be toxic. On the other hand, the cancer-fighting compounds were similar to those found in nature—in shrubs and herbs of the species astragalus. The next step is to find the most effective compound and test it in humans. However, the scientists warn that people should not try to treat themselves with selenium.



IS IT TIME TO JUNK THE WAY YOU USE COMPUTERS?

Re-engineering might cut costs to businesses by as much as 80%

Anyone who has bought a home knows what a pain it is to fill out all the forms needed to get a mortgage. But imagine what banks go through, processing all those forms from hundreds of customers a day, trying to weed out the bad risks but moving fast enough not to lose the good ones. "Traditionally, the mortgage business has been a one-to-one cottage industry" relying heavily on personal relationships within the bank, says J. Albert Smith, president of Banc One Mortgage, an Indianapolis-based subsidiary of giant Banc One Corp.

But in 1989, after two years of heady growth, the paper flow had become so crushing for Banc One that it figured something new was needed—radically new. Smith and his senior managers began rethinking the mortgage business from the ground up. As a result, Banc One is switching from a desk-to-desk assembly-line approach to a series of work cells similar to those used in building cars. Teams of about 17 people using computers convene electronically to work on all aspects of an application at once. They get the job done weeks faster than before. And team members are cross-trained. Smith says, so salespeople in the field—now equipped with laptops—no longer have to depend on an assigned loan processor.

FIRST, THE PROCESS. In the computer business, what Banc One did is called re-engineering. And it's the latest industry buzzword. The idea is so simple it seems obvious: Instead of using computers and information systems to automate the way a business has always run, you first re-engineer the process, then apply computing power to the new system. The resulting productivity gains are the best customers have seen from their computer invest-

ments in years. Re-engineering is "reducing costs by 80%, improving time to market by 80%, or doubling sales," says James F. Moore, president of GeoPartners Research Inc., a re-engineering consulting company. "Those metrics are what drives you to look at things in new ways."

Computer makers hope those measures will spur new sales. According to analysts, one reason for weak demand in the

computer industry, beyond recession, is that customers have automated virtually all the easy tasks they can find: payroll, financial accounting, and the like. IBM, Digital Equipment, Unisys, and Wang Laboratories all are seizing on re-engineering as a new marketing approach. So are systems integrators such as Electronic Data Systems and Andersen Consulting. Andersen, for instance, is advising Banc One Mortgage and other banks on how to re-engineer their businesses. G2 Research, a Mountain View (Calif.) market researcher, figures that re-engineering services were a \$5.4 billion business last year and will hit \$14.6 billion in 1995.

Re-engineering first surfaced in the 1980s in manufacturing circles. There, such concepts as concurrent engineering and just-in-time inventory-stocking and product deliveries demanded profound changes. These processes, all but impossible without sophisticated computer systems, upended traditional ways of doing things. Rather than isolate tasks into discrete departments, as they had since the Industrial Revolution, manufacturers began tearing down walls between engineering, manufacturing, sales, and support operations. That improved feedback from the marketplace and enabled more activities to take place in parallel, not sequential, order. Products got to market faster and with fewer defects.

Now, entire businesses are being re-engineered. That inevitably means new computers and software. "When you change how you work, it changes the way information is moved around," says GeoPartners' Moore. "It follows that you need to change your systems."

Hallmark Cards Inc. is using re-engineering to get new greeting cards, wrapping papers, and gift items to market sooner to meet customers' fast-changing



Instead of computerizing the way a business has always been run, the concept calls for rethinking operations

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Mr. Don Kott
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Information Processing

tes. The process now takes up to two years, but the goal is to get the job done in less than 12 months. Hallmark is setting up small teams of workers from its design, and sales departments to move products from concept to market. It also is bringing suppliers such as lithographers onto projects at earlier stages. And, to improve marketplace feedback, Hallmark is equipping its 100 retailers with computer-based cash registers, at no charge to the stores.

RE-ENGINEERING. "What has been automated over the past 20 to 30 years [reflects] how business was done over the past 20 to 30 years," says Donald Fletcher, division vice-president of business process redesign at Hallmark. "The computer systems we had were right for their time, not right for the future."

Re-engineering is now finding a strong following in service industries.

er data from different bank computers make it possible for customer-service representatives at a branch to get a complete picture of a customer's accounts and suggest new products.

Wang Laboratories Inc., which is struggling to stay afloat in the computer business by reselling IBM hardware, is pinning its hopes on re-engineering service businesses. Wang's specialty is electronic-image systems, which eliminate paper and speed the delivery of documents around an office. At Hartford Insurance Group, a Wang system has completely changed how the claims-processing department works. "Don't lay new technology on old cow paths," says Ronald J. Arenson, Wang's senior manager of image marketing. "Re-engineered work flow is the market."

IBM has hired one of the top re-engineering gurus, Michael Hammer, to boost its efforts in the new market. Hammer and his troops are training IBM salespeople in the re-engineering concept, both as a service and as a way to sell hardware. Hammer wrote a seminal *Harvard Business Review* article last year, titled "Reengineering Work: Don't Automate, Obliterate." Part of IBM's pitch is to show customers how re-engineering is helping Big Blue overcome its own business problems. Re-engineering is helping IBM's drive for what it is calling "market-driven quality." Beginning next June, the company's joint venture with Coopers & Lybrand, called Meritus Consulting Services, will begin selling re-engineering services.

Still, re-engineering may not deliver the boost computer makers seek. Companies should not confuse the addition of new computers with engineering technology, warns William A. Wheeler III, partner in charge of worldwide manufacturing strategies at Coopers & Lybrand. Technology "shouldn't be the driver," he says.

In some cases, re-engineering requires no new computer systems at all. Inland Steel Industries Inc. is in the midst of a major re-engineering project. But Bill Howard, vice-president for information technology, says he doesn't know if that will lead to more computers. "The focus has to change [from buying hardware] to fixing the processes," Howard says. "Once you get those right, then the existing technology may be adequate." That may send the computer industry searching for yet another buzzword.

By John W. Verity in New York and Gary McWilliams in Cambridge, Mass.

HOW THE APPROACH TO COMPUTING EVOLVED

AUTOMATION

1950s Using the new 'electronic brains' to mechanize routine office and factory procedures

MANAGEMENT INFORMATION SYSTEMS

1960s-1970s Collecting and organizing data for centralized analysis and control of the business

SYSTEMS INTEGRATION

1980s Connecting various brands and sizes of computers, often installed in different divisions or subsidiaries, to better share information

RE-ENGINEERING

1990s Rethinking business processes with the aim of cutting time-to-market for new products and services and really improving productivity

DATA. BW

banks, for instance, are striving to be more competitive, particularly when it comes to selling customers extra services such as loans and insurance. They aren't concerned only with cutting costs, says William E. Storts, managing partner of Andersen Consulting's retail financial services practice. And that, he says, means "organizing the work flow around the customer, not the product." Storts says that banks are now using their computers to capture data that can help them identify likely prospects for new business. Systems that pull togeth-

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TIME WARNER

AS DEBT WORRIES MOUNT, SO DO DOUBTS ABOUT STEVE ROSS'S STRATEGY

Steven J. Ross knows all about D-Day. This past June 6, the chairman of Time Warner Inc. was set to spring his own big surprise: a highly unorthodox \$3 billion rights offering. Ross should have had a premonition that things might go awry.

On another June 6, two years earlier,

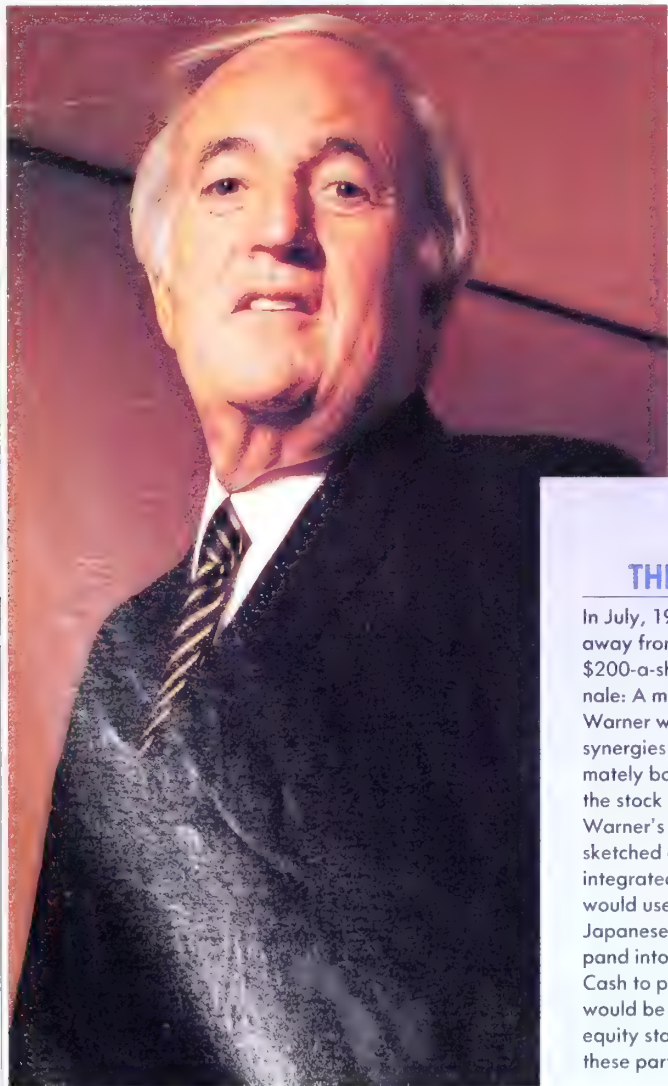
Ross's carefully fashioned merger of Warner Communications Inc. and Time Inc. was nearly unraveled by a phone call to Time Chairman J. Richard Munro. The caller: Martin S. Davis, chairman of Paramount Communications Inc. His message: Paramount would bid \$175 a share in cash for Time, scuttling Ross's cozy deal.

Ross and Munro won that battle, of course. By restructuring the deal so that Time would bid for Warner, they pulled off a merger in January, 1990. But the price of victory was steep: Besides angering shareholders, Time was forced to come up with cash to buy Warner, and the combined company

now lumbers under \$11.2 billion in debt. It's that crushing burden that forced Ross to ask shareholders to ante up more cash for the rights offering.

By this June, Ross was already taking heat on the Street for his 1990 compensation package, a gargantuan \$78.2 million. Shareholders' response to the rights issue was similarly unambiguous. They hated it. Within days, Time Warner's stock price tumbled from 117 to 88½—a sickening slide that knocked \$1.6 billion off the market value of its common stock. Investors still chafing from Time's rejection of the Paramount bid were now even angrier, branding the new offering coercive. "This is like Rape Two," says one major shareholder.

Beyond such bitter sentiments, some investors bear another lurking suspicion: that Steve Ross's ambitious vision of a vertically integrated media and entertainment conglomerate may be foundering on hard business realities. "We doubted the synergy. And we couldn't see the supposed benefits of the two



ALTHOUGH ROSS SEEKS A BIG GLOBAL ALLIANCE...

WHY TIME WARNER NEEDS

THE VISION

In July, 1989, Time walked away from Paramount's \$200-a-share bid. Its rationale: A merger with Warner would generate synergies that would ultimately boost the value of the stock even more. Warner's Steve Ross sketched out a vertically integrated company that would use European and Japanese partners to expand into foreign markets. Cash to pay down debt would be raised by selling equity stakes to some of these partners

THE PROBLEM

The synergies have been few. Businesses that thrived prior to the merger are still thriving. But there's little sign that they've benefited from the deal. What's more, Time Warner hasn't clinched a big strategic alliance. Few companies fit the profile for such a partnership. And Time Warner has had trouble agreeing with would-be partners on price and control for the deals. It's forging plenty of smaller deals, but these don't erase much of the \$11.2 billion debt

DATA: COMPANY REPORTS, BW

WHAT NOW

Time Warner must pay a \$4.3 billion term loan March, 1993. It can draw on a \$1 billion credit line to pay off part of the loan. That still leaves it hunting for \$3.3 billion. Cash flow won't cover it all. So Time Warner figures it must raise at least an additional \$1 billion. That can come either from a rights offering or from asset sales. The company has opted for the former, but its proposal infuriated shareholders, heightening scrutiny of its original vision for the me

companies in marketing and distribution capability," says Michael K. Arends, co-manager of Kemper Growth Fund, who sold off his shares after the merger.

No one is suggesting that Time Warner is starved for money: Its powerful cable television, music, and movie divisions generate more than \$1.7 billion a year in cash flow. But the billions more that Ross promised would come from the merger haven't materialized. And a close look at Time Warner suggests that that's because Ross's and Munro's original rationale for fusing the companies is fundamentally flawed.

BOBE-TROTTERING. The premise was that foreign markets open up to American media and entertainment products, a U.S.-based but truly global conglomerate such as Time Warner would stand to reap huge gains. The trick would be to forge massive alliances with partners in Europe and Asia who would help Time Warner crack these markets. Equally important, the partners would put up princely sums to get an equity stake in the Warner's rich assets, which range from Warner Brothers to *Time* magazine to Home Box Office (table). That money would go to pay down the debt—specifically, a \$4.3 billion term loan due March, 1993.

For 18 months, Ross has been scouring the globe for potential partners. He has been joined in this quest by Munro's successor as co-chief executive, N.J. Nicholas Jr., and Vice-Chairman Gerald Levin. So far, they've clinched only a flurry of much smaller deals. These include a joint venture with cable operator United International Holdings to develop a cable TV system in Hungary, as well as an agreement with French, Dutch, and German companies to distribute movies in Europe and the U.S. But despite talk-

ing to virtually every major media conglomerate and some consumer-electronics companies, the billion-dollar alliance has eluded Ross.

And there's the rub. Without an infusion of cash from a big strategic partner, Time Warner can't make that \$4.3 billion payment in 1993 (charts). While the company's operations are churning out plenty of cash, a combination of business trends and regulatory threats could soon cut into its margins. Since Ross desperately wants to avoid the draconian remedy of selling assets, he has little choice but to go to the market for more funds. "I think they need the money to repay the principal," says one unhappy shareholder. "They've tried to woo and win partners on a global basis, and they've come up short."

Ross has betrayed no hint of the strategy's weakness in discussions with money managers, analysts, and shareholders. Time Warner never intended to cover principal payments through cash flow. And the company insists that it won't back away from the rights offering. But Time Warner may ultimately modify the deal in response to investor concerns.

What don't they like about the offering? Under the current plan, Time Warner wants to raise \$2.1 billion to \$3.5 billion by offering shareholders rights to purchase 34.5 million shares. But the price isn't fixed: Each new share would cost

\$63 if only 60% of shareholders subscribe and up to \$105 if they all participate. So shareholders must cough up cash to maintain the same stake in the company—without knowing the cost, since the price they pay depends on how many play the game. And because shareholders who don't subscribe would see their holdings diluted, the deal twists their arms to buy in. "This is an unprecedented sum of money to be raised in an unprecedented way," says one investment banker. "It was a deal designed by a technician who put all the right levers and buttons on it to give it the highest chance of coercing shareholders."

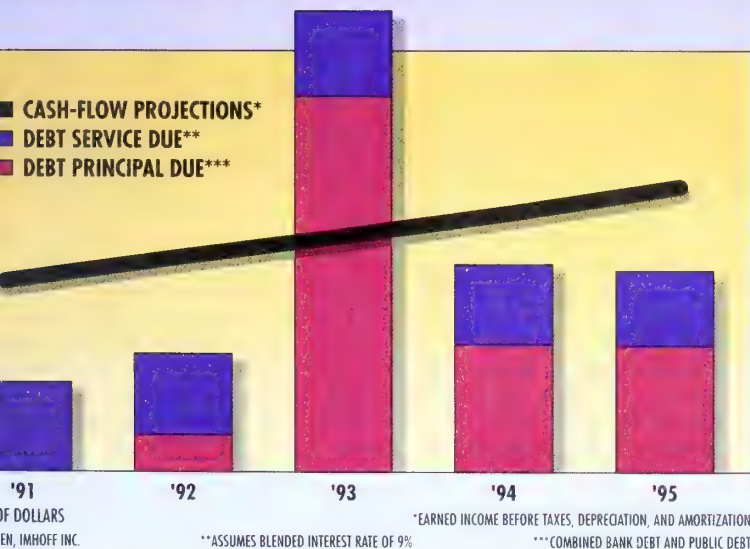
This time, shareholders aren't merely complaining. Fourteen suits have been filed challenging the plan, and some stockholders have protested to the Securities & Exchange Commission. They want the plan converted to a smaller, fixed-price rights issue. At the least, they want the price range lowered and narrowed. By July 10, Time Warner was beginning to show signs of relenting.

For now, Ross and Nicholas have plen-



... HE AND NICHOLAS HAVE JUST WON SMALL DEALS

INFUSION OF EQUITY



ty more to worry about. As both toured Europe recently to pitch the deal to investors, the burning question from shareholders was: Why haven't the strategic alliances happened?

Senior executives at Time Warner say prospective partners have been scared off by the debt, adding that they'll begin signing on once some of that weight has been lifted. But one investment banker familiar with Time Warner says that only two companies, Japan's Toshiba Corp. and France's Canal Plus, even got into serious discussions with the company. Canal Plus currently has a film distribution deal with Time Warner. But executives at the French pay-TV service say their company is too small to strike a meaningful strategic alliance with Time Warner. Toshiba says it passed on

prospective partners, according to bankers familiar with the talks. That reduces the number of would-be partners as well, since several oft-mentioned alliance candidates such as France's Hachette are struggling with their own finances. "Price will always be a matter of discussion," says the Time Warner executive, "but we are not arrogant." Exchange rates don't help, either: A weaker Japanese yen would make a deal tougher for Toshiba than Sony's 1989 buyout of Columbia Pictures or Matsushita's recent acquisition of MCA.

Even aside from economic vagaries or Time Warner's negotiating posture, few companies have the size and assets to

ble television markets: Witness the Hungarian cable venture and a new pay-TV service Time Warner recently launched with Svensk Filmindustri, Sweden's largest motion picture and TV producer.

Such deals work because government deregulation of European airwaves has generated an insatiable demand for programming. But the strategic alliances are tougher: A Toshiba deal, for example, would mean linking an electronic hardware manufacturer with a software supplier. Such linkups are attractive if the company wants to promote a new home-entertainment technology: Sony, for example, is putting movies from its RCA/Columbia Home Video unit on its eight-millimeter video system. Similarly, Pioneer Electronic Corp. has used an alliance with Carolco Pictures Inc. to pro-



TIME WARNER'S EMPIRE

Time's 1990 merger with Warner Communications created a media and entertainment powerhouse. Its publishing, music, and Home Box Office properties are the leaders in their businesses, while cable television and filmed entertainment are among the top three

1990 results; income figures reflect earnings before interest, taxes, depreciation, and amortization



MUSIC

22 major record labels, including Warner Bros., Atlantic, and Elektra; music publisher Warner/Chappell Music

STRENGTHS Broad array of superstars such as Madonna and Phil Collins; unparalleled global distribution system

WEAKNESSES Slack consumer demand; loss of lucrative distribution deals

REVENUES \$2.93 billion

OPERATING INCOME \$558 million

a proposal from Time Warner after it conducted a feasibility study. Neither company would discuss the outlines of the proposal.

Investment bankers in the U.S. say the Toshiba talks bogged down because Time Warner wouldn't relinquish any management control over the subsidiaries in which Toshiba was to acquire a stake. Time Warner insists it wants to install European-style management in its European ventures and Japanese-style management in Japan. Still, one Time Warner executive notes: "Depending on who our partner is, I don't think it's a good idea for them to come and tell us how the hell to make movies. We're too good at that."

Such unabashed confidence has led Time Warner to ask rich prices from

make such an alliance truly worthwhile. Arthur R. Barron, a former Paramount executive whom Ross lured from retirement last February to spearhead Time Warner's joint-venture effort, figures that eight companies in Europe and Japan meet the requirements. He adds, however, that offering Japanese and European partners a variety of equity stakes would swell the number of candidates appreciably.

INSATIABLE. Time Warner's smaller deals generally take two forms. The most common is one in which the company supplies its entertainment software—movies, TV shows, rights to licensed characters such as Bugs Bunny—to foreign programmers such as Canal Plus. The other is where Time Warner uses its technological expertise to create new ca-

PUBLISHING

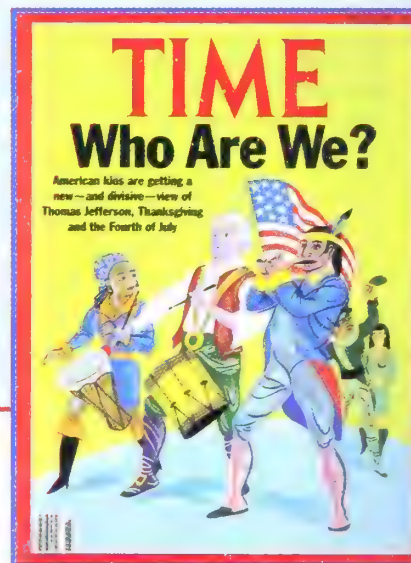
24 magazine titles, including *Time*, *Sports Illustrated*, *People*, *Fortune*, and *Money*; Book-of-the-Month Club; Little Brown & Co.

STRENGTH Three of the top five magazine titles in gross revenue

WEAKNESS Prolonged ad recession

REVENUES \$2.93 billion

OPERATING INCOME \$366 million



note its laser-disk technology. But Toshiba isn't a leader in such technology.

And some media experts contend that the appetite for these pairings is slackening. "I am not in the least bit convinced that there is a compelling reason for hardware-software alliances," says Robert Alexander, a consultant who has advised Time Warner and several other media companies. "I think it's a fad."

Such words don't daunt Barron. He says he has deals percolating in Greece and Britain, among other countries, and predicts he will close five or six more

year. He also insists that the Big Al still looms. And he adds that the pressure to produce a flurry of deals has increased because of the *Sturm und Drang* surrounding the rights offering: "We've never had anyone say to me, 'Why don't there more deals?'"

COURTROOM CAMERA. All of Time Warner's operating executives are quick to point out that the uproar hasn't led to pressure on them to jack up earnings. "It's not a mistake: The rights offering has turned a klieg light on the company's divisions. Simply put, investors are looking for signs of the synergies Ross and Munro promised when they talked up the merger 18 months ago. The company points to several areas where Time Warner's diversity

mits that innovative ad packages only go so far: "There is very little we can do to radically improve the short term."

Indeed, cash flow at Time's publishing division plunged from \$72 million in the first quarter of 1990 to \$42 million in the same quarter of 1991. That was the primary culprit in the slight decline in Time Warner's overall first-quarter cash flow, from \$536 million in 1990 to \$530 million in 1991. More revealing is that 1990 gross revenue was off 1.8% at *Fortune* and 2.7% at *Sports Illustrated*, according to Publishers Information Bureau. Revenue at *Time* was flat, while it increased 5.5% at *People*. These results are markedly similar to those of competing titles, in spite of Time Warner's ability to package a number of its publications or offer deals with other of its media properties. Media buyers on Madison Avenue say Brack's frustration with

dominated by hits. But Morgado says Warner has hedged its bets by nurturing a broad array of artists and styles. Last week, for example, Warner labels boasted 6 of the top 10 U.S. albums on the *Billboard* chart, with artists ranging from the heavy metal band Skid Row to pop crooner Natalie Cole.

HOODWINKED? Then there's Madonna, who is now demanding a multimedia deal with Warner to rival Michael Jackson's blockbuster pact with Sony Corp. Morgado won't comment, but Warner executives say privately that they doubt Madonna's appeal as a multimedia star. Still, Morgado had better hope the Material Girl keeps churning out hits: Madonna and other stars helped the music division kick in a hefty \$558 million in 1990



FILMED ENTERTAINMENT

er Bros. studio; television programmers
er Bros. and Lorimar Television; Warner
Video

STRENGTHS Only filmed-entertainment company that controls 100% of its worldwide distribution; *Robin Hood: Prince of Thieves* is shaping up as a hit

WEAKNESSES Inherently unpredictable business; future loss of some foreign TV syndication fees

REVENUES \$2.90 billion

OPERATING INCOME \$377 million

generated opportunities. But so far, the payoff is difficult to see.

Time Warner's huge cable system, for example, will certainly help Courtroom Television Network, a new channel backed by American Lawyer Media and the Warner Enterprises. The channel, which airs 24-hour coverage of trials, premiered July 1 on Time Warner's all-important Manhattan cable networks.

On the other hand, synergies have provided scant comfort to executives at the Warner's magazine division, who are coping with the worst advertising drought in two decades. Reginald K. Brack Jr., chairman of Time Warner Publishing, claims the merger has let him sell lucrative multimedia ad packages to clients such as Chrysler Corp. and General Motors Corp. But Brack ad-

CABLE

Warner Cable and 82%-owned American Television & Communications Corp.; basic-cable ventures such as Courtroom Television Network

STRENGTHS 6.5 million subscribers in key metropolitan areas such as New York City, and growing areas such as Florida

WEAKNESSES Big price hikes threaten consumer backlash, stricter government regulation; new technologies could open way to competitors

REVENUES \$1.75 billion

OPERATING INCOME \$769 million



the pace of package deals led him to realign his ad sales staff recently.

The maestro of Time Warner's huge music business is also waiting for an industry upturn. Robert J. Morgado, chairman of Warner Music Group, says weak demand for cassettes and compact disks contributed to a decline in first-quarter cash flow from \$149 million in 1990 to \$137 million. "We're going through a necessary readjustment to a slowdown in consumer spending," he says. Those results, however, weren't helped by the recent loss of distribution deals with Geffen Records and MCA, both of which were swallowed up by Matsushita Electric Industrial Co.

Music is an unpredictable business,



HOME BOX OFFICE

HBO and Cinemax pay-cable channels; basic-cable channels such as CTV; The Comedy Network; pay-per-view cable ventures such as all-boxing TVKO

STRENGTH Largest and highest-rated pay-cable service

WEAKNESS Pay-cable growth is slowing because of rising rates

REVENUES \$1.3 billion

OPERATING INCOME \$182 million

DATA: COMPANY REPORTS, BW

cash flow, making it second only to the cable division in profitability.

Warner's filmed entertainment division, with one of Hollywood's strongest libraries, generates more than \$370 million a year in cash flow as well. But it could do better, industry experts say. That's because to cut its risks, the company only produces about half the films it distributes. Its take from its summer hit, *Robin Hood: Prince of Thieves*, for example, would have been far greater if it had bankrolled the entire \$52 million in production costs. Instead, it only paid about one-fourth of the costs. So it has to watch the film's producer, Morgan Creek Productions, take the lion's share of profits.

As happened at the music division, Warner faces the loss of a deal to dis-

tribute Walt Disney Co. movies overseas. Yet Warner Brothers insiders put the loss of that business at less than \$30 million a year. And Chairman Robert A. Daly says he is already talking to other studios about picking up their business. More troubling is a recent Federal Communications Commission ruling that changes regulations governing fees from syndication of TV programs. The Big Three networks would share in some of the overseas revenues from shows they aired first. That would eventually damage the bottom line at the Warner Brothers and Lorimar TV units.

The shadow of government regulation hangs over Time Warner's robust cable holdings, too. Lobbyists in Washington are predicting that some form of further cable rereregulation will pass Congress this year. Now, broadcasters are pushing legislation that would force cable companies to pay a fee for the network feeds that they currently air on cable for free. Time Warner executives say the campaign will backfire on the networks: "It's so outrageous that it's hard to see it adopted as the law of the land," says Joseph J. Collins, chairman of Time Warner Cable Group.

FIRM FOCUS. Time Warner's weakest division is Home Box Office. While it's still the biggest and highest-rated pay cable service, HBO's growth has slowed from its heyday. It added 300,000 subscribers in 1990, a tiny fraction of its heady growth in the early 1980s, while sister channel Cinemax actually lost 100,000. So HBO Chairman Michael J. Fuchs is looking for new sources of revenue such as programming. HBO has begun distributing pay-per-view fare such as the recent Evander Holyfield-George Foreman heavyweight bout.

Rival media executives argue that Warner's already successful movie and music businesses have yet to benefit from the merger. Certainly, one result of the merger has been to introduce Time Warner executives to the financial jargon of a highly leveraged company.

Asked about his EBITDA results (earnings before interest, taxes, depreciation, and amortization, a common measure of a company's ability to meet its debt service), Morgado recently snapped: "Forget EBITDA. Let's look at the business."

He has a point. Time Warner owns a dazzling array of properties that have been solidly managed. And Steve Ross's dogged focus on global markets is logical enough. "We never doubted the globalization theory," says Kemper's

holders to suffer. "It's almost an oxymoron to say you're making money in Time Warner," says Dale M. Hanson, CEO of the California Public Employees' Retirement System, which owns more than \$5 million in Time Warner stock.

Hanson is one of several shareholders who are taking action. He has hired Providence Capital Inc., an investment bank that represents shareholders, to plead his case with Time Warner management. Rumors that the company

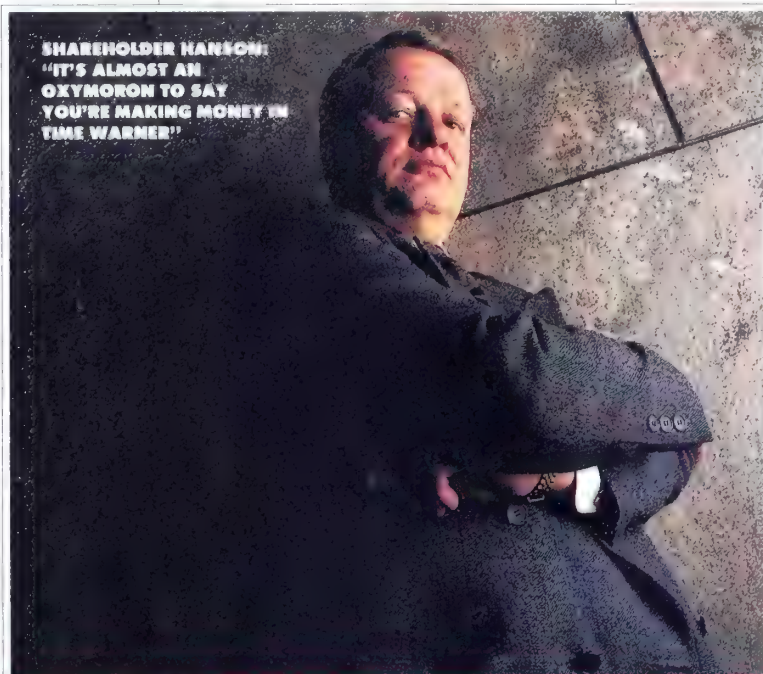
might bend sent Time Warner's stock up several times in early July.

BOXED IN. Most investment bankers still think the offering will fly in some form. Short of selling assets, it's unclear how else Time Warner would be able to pay off the \$4.3 billion term loan. Refinancing the debt would subject the company to steeper rates, since Time Warner negotiated its bank loans prior to the adoption of banking regulations governing highly leveraged transactions. "They would have to pay enormous fees to get that kind of financing this time around," says Gerald Hassell, executive vice-president of Bank of New York, one of Time Warner's banks.

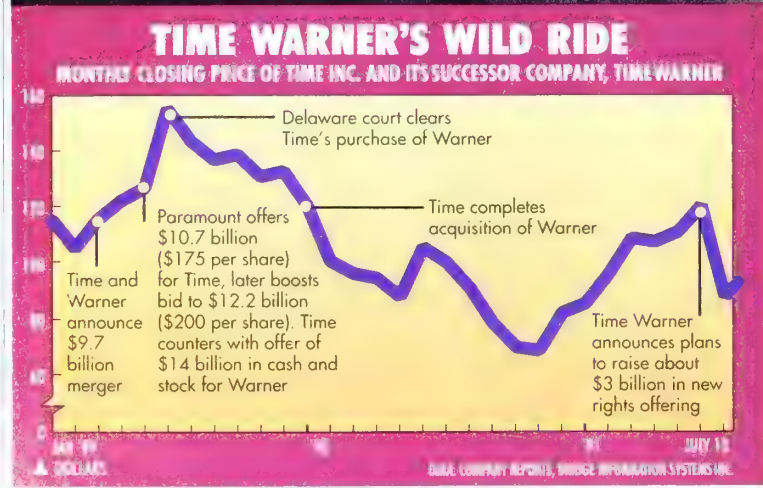
So Ross has boxed himself in. But he has a long history of wriggling out of tight corners: the devastating collapse of Warner's Atari subsidiary, his bitter feud with Chris-Craft Industries Inc. Chairman Herbert J. Siegel, Paramount's unexpected offer for Time. Shareholders may grumble and rivals may cluck, but few of them are betting that the ever-resourceful Ross won't extricate himself from this mess, too.

The bigger question has to do with Steve Ross's vaulting vision. Time Warner is in no imminent danger. But many shareholders of the world's largest communications company are starting to wonder: Is their money being mortgaged on a chimera?

By Mark Landler and Judith H. Dobrynski in New York, with Ronald Grover in Los Angeles, Mark Lewyn in Washington, and bureau reports



SHAREHOLDER HANSON:
"IT'S ALMOST AN
OXYMORON TO SAY
YOU'RE MAKING MONEY IN
TIME WARNER"



Arends. The trouble is that Ross bet shareholders' money on an overarching vision of how his businesses would fit into this global scheme. As Ross comes up short, Time Warner's shareholders must live with the fallout.

That above all has sparked the intense hostility toward Ross. A year and a half after denying investors Paramount's bid, which ultimately reached \$200 a share, Time Warner again is asking its share-

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PROCTER & GAMBLE: ON A SHORT LEASH

How the once-cautious giant wound up in FDA obedience school

For months, the Food & Drug Administration had been writing letters to Procter & Gamble Co., complaining that it was misleading to use the word "fresh" on Citrus Hill packages because the orange juice is made from concentrate. And despite a long day of meetings between agency and company representatives last spring, P&G still would not back down and remove the offending word.

Finally, at about 10:30 p.m. on an evening in April, P&G's people stalked out, apparently convinced that the FDA wouldn't take action. They were wrong. Within days, the FDA flexed its regulatory muscle by seizing a shipment of Citrus Hill. An embarrassed P&G quickly agreed to alter the labels. And just a few weeks later, the FDA forced it to take the words "no cholesterol" and a small heart off packaging for Crisco corn oil.

These high-profile incidents are only the latest in a string of setbacks the consumer-products giant has suffered recently at the FDA (table). P&G isn't the only company trying to cash in on the health craze by launching new products and making new claims. Nor is it the only marketer to be bitten by the newly aggressive watchdogs at the FDA. But P&G is feeling more scrutiny than most, because it has been making its health push across a broader array of categories—everything from prescription drugs to potato chips. It has run into obstacles partly because many of its products and claims are groundbreaking. It has also, by its own admission, mishandled some issues.

CRESTFALLEN. Procter's problems with the FDA are troubling—not just because 75% of its U.S. brands are in some way regulated by the agency but because P&G sees health and beauty products as a main engine for its U.S. growth. The company seemed ideally positioned to capitalize on health concerns. Be-

sides marketing muscle, it has plenty of technological prowess. So it could ultimately benefit from a stricter FDA that would permit health claims only from companies with the science to back them up. In the meantime, though, its recent reversals are holding up growth in the company's U.S. business, where unit volume shrank 4% in the first quarter.

P&G's most costly misstep may have been its botched attempt to gain FDA approval for a new version of Crest toothpaste. The company asked for permission to launch Ultra Protection Crest, formulated with triclosan, an antimicrobial agent that is sold in toothpastes abroad as a plaque-

fighter. P&G told the FDA that its proposed label would make only cosmetic claims. But at an October meeting of the American Dental Assn., Procter promoted the toothpaste's "antibacterial efficacy," raising eyebrows at the FDA. P&G later backpedaled, but it was too late: In February, the company aborted its launch of the toothpaste after the agency said it planned to consider it a new drug, requiring clinical studies and time-consuming application process.

P&G's woes are partly the result of an unfortunate coincidence. Just as the FDA has grown more watchful, the company long known for its ultracautious style has become more aggressive. "They've been willing to be a little faster, with a little more gutsy approach," notes a regulatory expert at one rival. In the case of Citrus Hill, though, bad luck may also have been to blame. Procter "just happened to be in the wrong place at the wrong time," says Peter Barton Hutt, a

former FDA chief counsel. Agency officials acknowledge they were looking for a visible target to show they were serious about misleading labeling, and orange juice was a good one.

NONFAT CHANCE. The story is more complex for olestra, the fat substitute that the FDA has been pondering for more than four years. No previous food additive has had the potential to be consumed in the quantity that olestra might, so the FDA has had to develop a new standard to test its safety. And while P&G has made a good deal of headway, the company is still doing research on olestra's effects in the body. "The olestra case is precedent-setting. It has to be approached very carefully," says F. Edward Scarbrough, acting director of the FDA's Nutrition & Food Sciences Office.

If P&G is having problems with olestra, a drug-like food, it also faces them with its fiber laxative Metamucil, a food-like drug. Four years ago, Procter asked the FDA for permission to tell consumers that psyllium, the active ingredient in Metamucil, helps lower blood cholesterol. Some research has shown it does just that, albeit modestly. The agency said it needed more data, which P&G is now producing. But competitors may get a head start. As part of new nutrition labeling rules that will be in place by 1993, the FDA could permit cholesterol-reduction claims by cereals containing psyllium.

Competition also is an issue

P&G'S HEALTH PITCH HITS SOME SNAGS



ULTRA PROTECTION CREST Halted national launch after FDA said new toothpaste with an antibacterial agent required new-drug approval



CITRUS HILL FRESH CHOICE Agreed to drop 'fresh' from name after FDA seized some of the orange juice, saying the labeling was false and misleading



CRISCO CORN OIL Dropped 'no cholesterol' labels from all its food products after FDA told vegetable-oil marketers to stop using the claim



METAMUCIL Doing clinical research to support cholesterol-reduction claims for this fiber laxative after FDA asked for more data



DIDRONEL Awaiting FDA approval to market this prescription drug as an osteoporosis treatment—but an advisory panel has questioned some of the data



OLESTRA Still hasn't won FDA's go-ahead four years after its initial petition to sell this fat substitute

DATA: BW

ONE LEADER SALUTES THREE OTHERS

For the past fifteen years, Business Week has recognized outstanding leadership in the truck industry by conferring the Truck Dealer of the Year Award. We do this in association with the American Truck Dealers. In addition to the Grand National Award, we are honoring three finalists, who were

chosen from twelve nominees. These finalists are Mr. Robert S. McCoy, President of Truck Country of Wisconsin, Inc. in Madison, WI; Mr. Gareth H. Mitchell, President of Motor Truck Equipment Co. in Carlisle, PA; and Mr. Ernest A. Speno, President of Mission Valley Ford Truck Sales, Inc. in San Jose, CA.

All three gentlemen were selected by Business Week in conjunction with the Columbia University Graduate

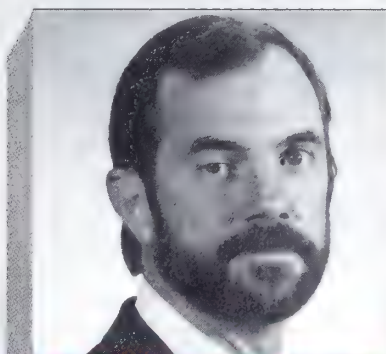
School of Business in recognition of their successful dealerships and outstanding civic contributions. Business Week proudly salutes Mr. Robert S. McCoy, Mr. Gareth H. Mitchell, and Mr. Ernest A. Speno, the 1991 Business Week/ATD Truck Dealer of the Year Finalists.



Mr. Robert S. McCoy

**1991 TRUCK DEALER
OF THE YEAR**

FINALIST



Mr. Gareth H. Mitchell

**1991 TRUCK DEALER
OF THE YEAR**

FINALIST



Ernest A. Speno

**1991 TRUCK DEALER
OF THE YEAR**

FINALIST

drug, Didronel, which has long been used to treat a bone ailment called Paget's disease, P&G asked last year that it be approved as a treatment for osteoporosis, the bone disease that afflicts more than 20 million U.S. women. Some analysts have it pegged as a \$500 million drug.

However, some members of an FDA advisory panel that met in March voiced concerns over the latest research, which indicated a possible reversal of earlier benefits as therapy continued. P&G Vice-President Geoffrey Place sees this as a "statistical wobble" and says evidence for the drug is solid. But the new questions could cause Didronel to lose ground to other similar drugs under development. "It's very important to P&G to get this going quickly because there are two drugs not far behind," notes independent analyst Hemant K. Shah.

'SHORT-TERM' SNAGS. Despite P&G's numerous regulatory headaches, no one sees any attempt by the FDA to single out the company. Place concedes that P&G has been "ineffective" in some of its dealings with the FDA, although he says the snags are "a short-term, tactical issue which will not affect our long-term relationship or our ability to build our business." Even so, P&G Chairman Edwin L. Artzt is unhappy over the way the food-labeling issue was handled. "Some of it could have been avoided," he says. Some analysts and former P&Gers believe that the June resignation of B. Jürgen Hintz, the P&G executive vice-president responsible for the food and beverage business, reflected in part that displeasure.

P&G set up a new worldwide organization to handle regulatory issues last November, and Place believes that it will soon prove its mettle in Washington. He expects the FDA to approve Didronel for osteoporosis, and new prescription drugs for inflammatory bowel disease and urinary tract infections, in less than the two or three years the agency normally takes. P&G filed for the drugs in 1990.

Other tests of P&G's regulatory relations are nearing. Later this month, the FDA will consider whether the stomach remedy Pepto-Bismol can continue to be marketed to treat diarrhea. And if partner Syntex can gain FDA approval, P&G hopes to sell Syntex's top-selling antiarthritic drug, Naprosyn, in over-the-counter form. Another petition just filed at the FDA asks it to affirm as safe a low-calorie fat called caprenin, which P&G hopes to sell as a substitute for cocoa butter in confections. How these and other health items fare will have a great impact on P&G's own health.

By Zachary Schiller in Cleveland and



PUBLISHER LAVENTHOL: CIRCULATION HAS CLIMBED TO MORE THAN 1.2 MILLION

A FREE NEWSPAPER WITH EVERY CABLE-TV GUIDE

How the *L.A. Times* finally turned the tide in Orange County

Newsroom smart alecks called it Vietnam. That's how swampy the battle had grown in California's Orange County for the *Los Angeles Times*. Lured by the county's growth and a median family income that this year may top \$56,000, the *Times* tried to gain on *The Orange County Register*. Yet from 1979 to 1989, as the *Register's* daily circulation in the county soared 56%, the *Times's* grew 3%. By 1989, the *Register* was selling more than 135,000 more Sunday papers than a decade earlier; the *Times*, just 909 more.

Well, you can forget Vietnam now. In the nearly two years since Publisher David Laventhol took command and Editor Shelby Coffey III unveiled a front-to-back makeover, total circulation of the nation's largest metropolitan daily has climbed approximately 12%, to more than 1.2 million. More heartening, the *Times* saw daily circulation in Orange County increase 11%—and a phenomenal 26% on Sunday (chart). The *Register*, while holding its lead, grew only about 7.5%. This is all a dramatic reversal of a trend in which suburban dailies have been blunting the spread of large, estab-

lished papers beyond their core markets.

Was it the *Times's* new "faster format," which offers news digests on each section front? Or its coverage of the gulf war, which Laventhol says was "as good as the *Times* has ever done"? Or the death of rival *Los Angeles Herald Examiner* in 1989? All of those helped. But the *Times's* killer weapon proved to be as unlikely as it was deadly—a revamped Sunday television guide geared to a reader's own cable-TV service and the patchwork of cable networks in the L.A. area. "Their cable book has cost us a lot of money," says *Register* circulation chief Patrick H. Elster.

For all its 27 foreign bureaus and growing international prestige, the *Times* is paying as much or more attention to Costa Mesa as Nicosia. As part of that strategy, the paper a few years back began signing up cable operators in Orange County and the San Fernando Valley, home of another competitor, the *Daily News*. Now, every household in those areas can get the *Times's* weekly *TV Times*, the official customized guide to local cable programming. It's an easy sell: Viewers need just one guide to

ow what channel in their
ea carries, say, ESPN, which
ferent cable systems put
different channels. One
mes executive reckons that
ce its debut in February,
90, the guide was responsi-
for signing 90% of the
nday Times's new Orange
ounty subscribers.

The cable book slammed
e a cruise missile into the
gister, which rushed to
do its own guide. "For the
st time in 10 years, they're
acting to us," crows the Ti-
es's Orange County Edition
resident Lawrence M.
gby. That name may ring a
l: Higby served as an aide
the Nixon White House
ring Watergate. In the book *All the*

resident's Men, Deep Throat dismisses
n as "a young-punk nobody who does
at he is told." But from there, Higby
ent 10 years at PepsiCo in marketing
fore joining the Times's cable-TV affilia-
e. He moved to the paper in 1989,
ere he helped engineer the makeover
TV Times. Years of selling soft drinks
ve clearly left an impression. Says
gby: "We treated the paper like you
uld treat any new consumer product,
d guess what? It worked."

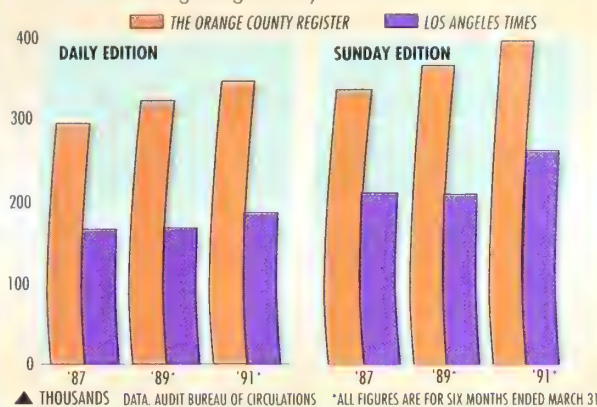
AGGERING. Still unknown is whether
e paper can turn its new readers into
ash earnings. With a market it sees
etching across California from Santa
rbara to San Diego, the paper must
ep facing down 41 smaller rivals. And
ht now, each is competing for ads in a
wspaper slump Laventhol calls "the
rst in memory." Even with higher cir-
ulation, first-quarter newspaper reve-
e at parent Times Mirror Co. sank 7%,
\$479.1 million. Operating profit for
e group, of which the Times makes up
out half, plunged 73%, to \$14.8 million.
Withering profits have employees
arrying. Laventhol says he plans no
roffs, though the Times has a hiring
eze in place. The paper's total adver-
ing fell 18.8% in the first five months
1991. So unless ads rebound

partly, it may be some time be-
re the Times's investment in
ulation pays off. Told of the
s Angeles Times's circula-
n gains, Arthur Ochs Sulz-
rger Jr., deputy publisher of
e New York Times, jabs:
ood for them. I wonder how
ach it's costing?"

Excellent question—and one
venthol isn't answering. But
look at how the Times has
ilt circulation in key areas
uggests the new readers are
osting plenty. In Orange
ounty, the paper doubled the

THE BATTLE FOR ORANGE COUNTY

The Orange County Register still tops The Los Angeles Times in average circulation and advertising volume in Orange County. But The Times is gaining Sunday circulation



ranks of workers selling subscriptions. At its two circulation offices in the county, the Times has installed a state-of-the-art automated dialing system developed by Rockwell International Corp. With two shifts of 32 solicitors working 12 hours a day, the system can make 4,800 contacts a day. Delivery agents also leave free samples of the paper on thousands of doorsteps in Orange County. Later, salespeople are sent door-to-door to call on these homes.

The Times is also slashing subscription rates: New subscribers can get the paper daily and Sunday at 40% off the usual four-week rate of \$11.40. The Register discounts, too, but in April, it boosted its nominal monthly rate for Sunday and daily delivery by \$1.50, to \$9. A month earlier, the Times had exempted Orange County from an 8.8% subscription increase it had slapped on readers in other areas.

But those selling costs add up to mere nickels and dimes next to what the revamped *TV Times* costs. The paper had to pay cable operators to land multiyear contracts that designate the Times as

their official guide. Laventhol won't disclose how much, but the Register's Elster says he dropped out of the bidding for one system after the Times "threw out some figures that were pretty staggering." *Daily News* Publisher David J. Auger claims he abandoned hope of tying up other cable systems once the Times bid over \$500,000. "They shelled out huge amounts," he says.

Because the Times moved silently at first, most of its deals with cable operators probably didn't cost nearly that much. To ensure that the 14 different editions of *TV Times* reach the right readers, the paper had to work

with dozens of delivery agents to redraw delivery zones. The Times must also pay extra to publish 14 distinct TV magazines. And it's forgoing circulation revenue from cable viewers who choose to subscribe through their cable operator. Those readers get the Sunday paper for 50¢ a week, not the ordinary \$1 price.

An immediate payoff is not in sight. Lynch, Jones & Ryan Inc.'s John Morton worries that even in a recovery, retail ads—a Times mainstay—won't bounce back to previous levels. Nor do rivals see a quick end to the ad slump. "Our basic business plan assumes a continued depressed, recessed economy," says Register Publisher R. David Threshie.

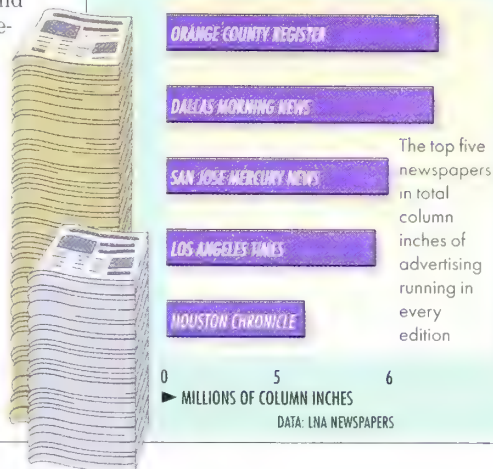
Willard Colston, the Times's director of development, takes the long view of the *TV Times* investment. "It will pay out better when the economy improves," he says, adding, "it's pretty hard to be a newspaper without circulation." Higby claims the extra circulation is paying off already. Twice in the past year, he says, the Times boosted ad rates higher than it could have with fewer readers.

Whether those hikes also acted to suppress demand for ad space is a matter of conjecture. Meanwhile, Higby's rivals won't call a truce on the circulation front. The *Daily News* has fielded 130 new door-to-door solicitors. And the Register has slashed its rates, too, to build its daily circulation margin over the Times to a record 160,754.

Yet Laventhol points to the latest Sunday numbers, which show the Times still gaining in market share on the most important advertising day of the week. As for Higby, he seems anything but crushed. After his tour of duty in Orange County, Laventhol promoted him and gave him the extra job of circulation chief for the whole paper. Not bad for a "young-punk nobody"—and a sure sign that the Times will stay fiercely competitive in the war for Orange County.

By Robert Barker in Los Angeles

U.S. ADVERTISING POWERHOUSES



SO YOU WANNA OWN A BASEBALL TEAM

Before you write a check, ponder Tom Werner's rude awakening

Before he bought the San Diego Padres in June, 1990, television producer Tom Werner loved to play rotisserie-league baseball, "owning" an imaginary team composed of major-league stars. Owning the real thing isn't always as much fun.

A month after he and 14 partners closed their \$75 million deal to buy the Padres, Werner watched in horror as Roseanne Barr, star of his hit series *Roseanne*, screeched and scratched her way through the National Anthem. His first year as an owner also featured a still-simmering salary dispute with All-Star catcher Benito Santiago, open feuding between stars Tony Gwynn and Jack Clark, and a front-office purge. "I'm glad that year is over," says Werner. "I've learned that baseball is a tough, bottom-line business."

NEW LOOK. To its owner's evident relief, the team's future looks better than its past, even though the Padres, as of the All-Star break, are in fourth place, 10½ games behind the Los Angeles Dodgers in the National League's tough Western Div. Werner, who parlayed *The Cosby Show* into a sizable fortune, is remaking the team from top to bottom. "It was a dormant operation, too conservative," says Michael Megna, a sports-valuation expert for American Appraiser Inc.

No longer. Out went the dreary,

brown-trimmed uniforms, in came classy blue pinstripes. Sayonara, General Manager "Trader" Jack McKeon and 40 other front-office employees. Later for you, Clark: Feel free to do your righthanded power-hitting for the Boston Red Sox from now on.

To retain the team's most marketable players and develop new talent, Werner, 41, brought in Joe McIlvaine, late of the New York Mets. McIlvaine traded slugger Joe Carter and promising second baseman Roberto Alomar to Toronto for first baseman Fred McGriff and shortstop Tony Fernandez. And he shelled out nearly \$40 million to sign multiyear deals with McGriff, hitting machine Gwynn, and pitcher Bruce Hurst.

McIlvaine's moves, which sent payroll costs up 30%, to \$21.7 million, are already showing results. McGriff has 16 home runs, tying him for second in the National League. Gwynn is the league's leading hitter, with a .358 average. Hurst could become the team's first 20-game winner since 1978.

The clubhouse isn't all smiles, though. Santiago, 26, isn't satisfied with the Padres' offer of \$11 million over four years and could become a free agent after next year. The friction

highlights a long-term problem for Werner and McIlvaine: Teams in larger TV markets can generate more revenues than the Padres, so Werner needs to keep down payroll costs. To that end, the Padres have increased their minor-league budget and added scouts.

ROCK CONCERTS. But there's more to running a team than spending big on a few stars and pinching pennies elsewhere. Perhaps Werner's biggest task is to get the turnstiles clicking. Even after raising ticket prices by as much as \$1.50, to a top price of \$11, and hiking parking \$1, to \$4, the Padres will be lucky to break even on more than \$40 million in revenues, says club President Dick Freeman. The St. Louis Cardinals, by contrast, bring in some \$56 million a season. To draw crowds, Werner has added post-game rock concerts, targeted ads to San Diego's large Hispanic community, and improved ballpark food.

The real money in team ownership, though, is often in the appreciation of franchise value, not operating profits. And, says Megna, partly because the \$95 million entry price for the two new NL expansion clubs set a floor price for franchises, the Padres are now probably worth \$100 million. "That's if someone wanted to buy it," says Werner quickly. "And I'm not selling." But hey, after a first year like Werner had, he's earned the right to have a little fun.

By Ronald Grover in San Diego

Werner of the Padres: 'Baseball is a tough, bottom-line business'



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WHAT'S THIS? AMERICAN CARS GAINING IN JAPAN?

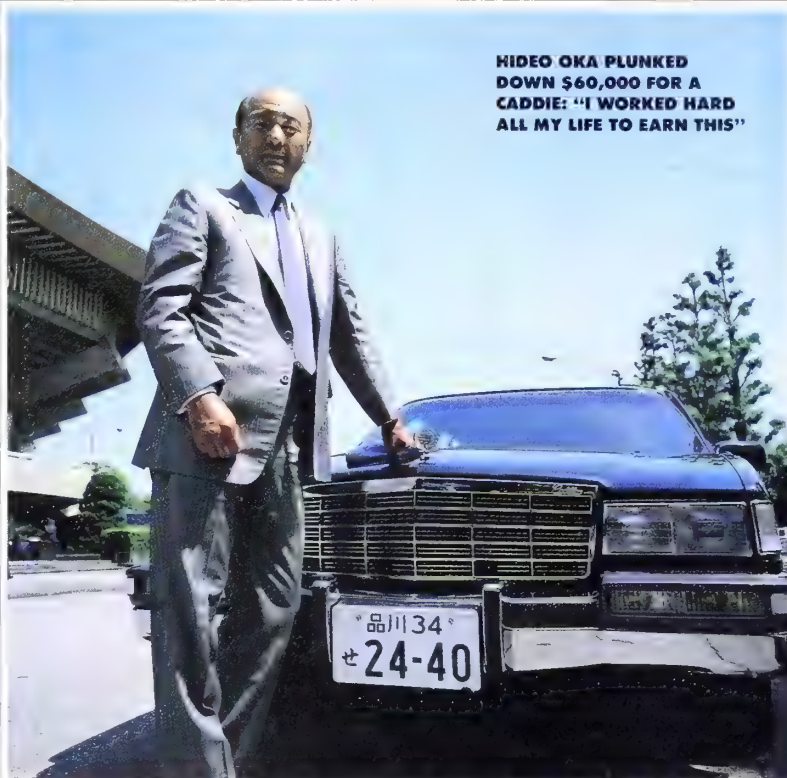
They still get double takes, but Detroit iron is building a tiny following—left-side steering and all

When Hideo Oka got his driver's license at age 20, a big American car was an impossible dream. So he settled for an Isuzu. Finally, in 1985, he bought a used Cadillac. And this year, he splurged on a new Fleetwood—\$60,000 in Japan. The Tokyo dentist, now 55, proudly maneuvers his Caddie to work and to tennis or mountain-bike trails on weekends. "I worked hard all my life to earn this," he says.

What's that? Detroit iron a status symbol in Japan? Don't be so shocked. U.S. cars are still rare there, but appeal to a growing coterie of loyal customers. And those so bold as to own Ame-shas, as they're known, often love 'em. "It's easier to drive," says Haruo Morioka, 61, a Mercedes fan until her husband gave her a 1990 Chrysler New Yorker. "I was surprised."

From a tiny base, Detroit is making progress in Japan. The Big Three's sales have climbed 800% since 1985 and this year could top 1979's record 16,709 units—even as Japanese imports of foreign-made cars are running 13% behind a year ago. The gains are relative: Total imports to Japan were 221,706 cars last year, including 128,832 from BMW, Daimler Benz, and Volkswagen-Audi. And those numbers are dwarfed by the 3.3 million cars and trucks the Japanese sold in the U.S. Still, General Motors and Chrysler are recovering—and Ford is trying to—from a dizzying decline in Japan in the early 1980s. Back then, poor gas mileage and quality demolished Japanese sales of U.S. cars. Even Tokyo gangsters traded in their cream-colored Lincolns for Mercedes.

The Big Three haven't yet dealt with

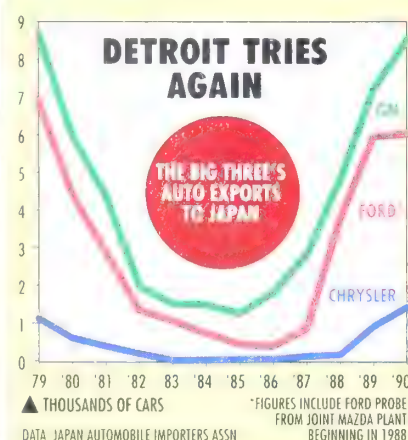


all the problems that led to this debacle. Rather than setting up dealerships, as the Germans have, they still rely heavily on importers to sell their cars. Moreover, they simply ship over U.S. models "as is"—with steering on the left instead of on the right, Japanese-style. That limits sales mainly to those who consider left-

Japanese drivers, but that car probably won't reach Tokyo docks until 1993. Ford's Explorer is a hot seller in the U.S., but exports to Japan started only in October—through seven small Japanese companies. Sales so far: 145.

PERSONAL STATEMENT. Still, many of the factors that hurt Detroit are being addressed. Duties on imports ended in 1978. Washington is pushing Tokyo to deal with informal barriers such as a distribution system that keeps most dealers loyal to one manufacturer, who often provides such perks as loans, showroom remodeling, and training. Moreover, U.S. producers have raised the quality and mileage of their cars nearly to Japanese levels. And U.S. models are often safer than Japan's domestic ones. James Steinhagen, General Motors Japan Ltd.'s vice-president for marketing, sales, and service, argues that Japanese consumers don't know yet how much U.S. cars have improved.

Indeed, Japanese who try U.S. cars



the styling and zip. Last year, Fumio Maruyama, 42, bought a Jeep Cherokee. The film lighting technician found a hole in the muffler, and sometimes the engine goes kacha-kacha. But for a car that's powerful yet compact, "it's worth it," he says. Magazine editor Kumiko Kato says many Japanese consider American cars "a way to express ourselves." Not that playing to Japanese consumers is a snap. To clinch a sale, BMW will rent a car to match a customer's favorite dress. Salespeople try to lock buyers for life, contacting them often and on weekends and at New Year's. Tokyo florist Sachiko Yamada, 40, is on her fifth Nissan. She likes Corvettes, but she inherited her Nissan salesman from her father and feels "too obligated to switch."

TIGHT TIES. The Germans are stepping up the pace to deal with all this. Since 1981, BMW has poured \$100 million into a network of 122 exclusive dealers who sold 36,527 cars last year. Mercedes and Volkswagen are also setting up their own dealerships, while spending about \$100 million each on new centers that go over imports to make sure they're shipshape for Japan's demanding equipment standards and buyers. Mercedes has also teamed up with Mitsubishi to sell some models, while VW expects to sell some of its cars through Toyota.

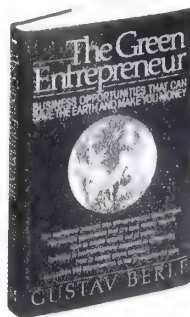
Detroit, by comparison, is taking baby steps. GM hopes to boost its exports to Japan by 17% this year, to 10,000. It has just upgraded its Tokyo office to a subsidiary and is pushing some models with its own ads. But it plans to keep selling through its distributor, Yanase & Co. Chrysler has tripled its dealer network since creating a Japanese sales organization three years ago that is 85% owned by the trading house J. Osawa & Co. But it still has just 45 outlets.

Ford has done the most to build its brand. Mazda Motor Corp., in which Ford holds a 25% stake, sold some 82,000 cars with Ford nameplates last year. Ford also has bought 34% of Mazda's Autorama, a 334-outlet chain that mostly sells Mazda-built Fords. But U.S.-made Fords aren't doing well. Sales of the Probe, made in Michigan with Mazda, fell 41.3%, to 1,588, in the first three months of 1991—largely, Ford contends, because the car looks dated. A redesigned model is due next summer. Meanwhile, Ford hopes that a former Toyota executive it just named president will give its subsidiary a boost.

The Big Three can't afford to be laggards much longer. The newest developments in autos now often appear in Japan first. So to defend its home turf, Detroit has to compete over there. And that means going after more than a few over-the-hill dentists.

By Karen Lowry Miller in Tokyo

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FINANCES CAN BE TRICKIER THE SECOND TIME AROUND

Deena Katz, a financial planner, and her partner, Harold Evensky, were in California on business last year when Katz suggested a side trip to the Napa Valley. There they were, at a romantic little vineyard, when Evensky dropped on one knee and proposed. Then, he popped the really important question: "Should we sign a prenuptial agreement?"

"Don't be ridiculous!" replied Katz, even though she was the wealthier of the pair. It was a surprising reaction from someone who had unfailingly counseled her clients to "make him sign that prenup." But Katz, who like Evensky was divorced, soon changed her mind. "It's very difficult to separate the love relationship from the very necessary things you have to do, like putting your finances together," she says.

HIGH STAKES. That's the trouble with mixing love and money. Many people fear that talking about money at such a time makes them appear greedy and may douse the romance. Yet the stakes are high—especially the second time around. Premarital financial planning is important for any couple. But it's crucial for those about to remarry. Generally, they are older, have more assets, and have more complicated finances than those tying the knot for the first time.

They must ask themselves: What do they do with assets they've accumulated separately? How will they deal with children from previous marriages? How should they combine current earnings?

Couples who ignore these issues increase the chances of another failed marriage. But

airing them in advance and laying some ground rules can pay off. To begin with, you'll need a thorough understanding of the legal status of prenuptial agreements in the state where you'll reside.

Before you consult a lawyer, take a look at the way you and your prospective spouse handle money. Even if you don't want to discuss who will buy the groceries and pay the electric bill, planners suggest you map out a broad financial policy and proceed slowly in combining assets.

Even though keeping separate accounts may go against the grain of togetherness, maintaining financial independence can help you establish a better relationship. Besides, once your property is commingled, it's much tougher to disentangle should that become necessary. Most planners suggest that partners retain sole ownership of property they hold at the time of their marriage. "Other than a home and checking account, I don't

payments being received from a former spouse will stop at remarriage. And you should talk about how much each spouse will contribute and how bills will be paid. Most planners suggest using a



household account for common needs. You'll sometimes need to go over what will be contributed to it and what will be paid from it. Connie Chen, managing director at Richard A. Eisner in New York, suggests you start by splitting contributions down the middle. "But as time goes on, the one who makes more money may want to contribute more," she says. Planners suggest you also discuss who will handle long-term investments, who will pay bills, and who will collect tax data.

It's a good idea to rethink your diversification strategies and liquidity needs. Barbara Pope, partner in charge of personal financial planning for Price Waterhouse in Chicago, says her husband's practice of staying liquid and keeping a lot of cash allows her to stay fully invested. "If I'm desperate for cash, I can get it from him," she says. Even if you maintain separate portfolios, make sure each partner understands the oth-

er's holdings and would feel comfortable managing them in case of the spouse's illness or death, says Violet Woodhouse, a financial planner in Costa Mesa, Calif.

State and federal tax liabilities will have an obvious impact on your new financial situation. If you and your spouse have widely disparate incomes, or if one of you does not have any earned income, you will probably pay less in taxes as a married couple. But if remarriage will make you part of a two-earner family with each making substantially equal amounts, expect your tax bill to go up.

KID STUFF. Another consideration is the onetime \$125,000 capital-gains exclusion available to taxpayers 55 years and older who sell their primary residences. If you marry someone who has used the exclusion, you cannot use yours. Pope suggests that you or your spouse may want to sell a home before you marry to take advantage of the exclusion.

It's also crucial to accommodate the children from prior marriages. If they are still living at home, it's especially important to iron out money issues well before the wedding ceremony. "These are not big financial issues, but they're huge emotional issues," says Kenneth Davis, a Menlo Park (Calif.) stockbroker who wrote the book *Kids and Cash*. "A simple disagreement over whether you should pay a child an allowance can result in a huge family battle."

Once you've decided to draw up a prenuptial agreement, you and your new spouse will each need an at-



think anything should be held in joint names," says Paul Huth, partner at Ernst & Young in Cleveland.

Couples who remarry need to think through their anticipated cash flow. Any alimony



ney if the agreement is pass muster in most state courts, says Sam Radin, president of National Madison Group, estate planners in New York. Each of you must provide full disclosure of your assets and liabilities so that the party giving up rights will know what is being surrendered.

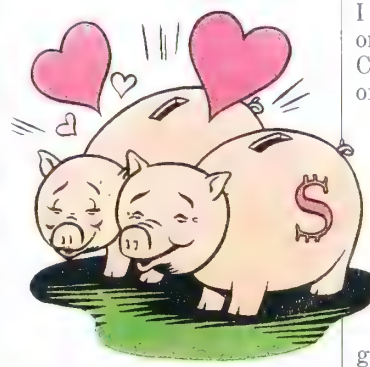
LIVED RIGHTS. In community-property states, the law considers property brought to the marriage as separate, but if it increases in value, is improved, or if taxes or upkeep are paid out of community funds, the increase could go to both partners unless an agreement delineates the ownership. A prenuptial agreement can identify the property as separate and

waive all potential community-property rights.

Although planners counsel against joint ownership, there should be something at stake for the two of you as a couple, too. Stuart Walzer, a divorce lawyer with Walzer & Gabrielson in Los Angeles, counsels against separating everything in a prenuptial agreement. He argues, for example, that the increase in value on property that is separately owned should be shared equally by both spouses. "Marriage is partly about money and security and about working together to accumulate something," says Walzer, who has taught a course for lawyers on second marriages. An agreement that undermines this team

spirit may "doom the marriage before it starts."

Another option is to hold property as "tenants in common." This allows you to split property according to designated percentages and provides that your portion will pass to your heirs at your



death. For example, you can say one spouse owns 10% of a house, the other, 90%.

You don't have to complete your estate planning before the wedding, but it may ease tension between your children and new spouse if you make financial and estate plans clear. That's especially true of people with adult children, who often have legitimate concerns about the new person in their parent's life. "If the natural parent dies, the stepparent has no legal obligation to provide for the stepchild," says Woodhouse.

One way to provide for your children is to buy a life-insurance policy and keep the proceeds out of your estate. Make your children owners of the policy. You can give them the money to pay the premiums, using the \$10,000 annual gift exclusion.

UNLIMITED DEDUCTION. Another estate-planning tool is a qualified terminable-interest-property trust (QTIP). This allows you to use the unlimited marital deduction, under which your entire estate can pass to your spouse tax-free. But you can still control the ultimate disposition of your assets. You can leave your estate in trust, with the income—and perhaps some of the principal—going to your spouse. But the bulk of it passes to your children when the spouse dies. If you are a business owner, Fort Worth estate-planning lawyer Michael Bourland adds, you may need more sophisticated planning to be certain your children inherit your business.

Once an agreement is reached, couples seem to feel the effort was worthwhile. "Some of the happiest people I deal with are those in second marriages," says Carol Caruthers, partner in charge of personal financial services for Price Waterhouse in St. Louis. "Because they've been in a situation that didn't work so well, they don't take the marriage for granted." Clearing up financial concerns early on paves the way for a happier second go-round. *Mary Rowland*

Travel

MORE MILEAGE FROM YOUR CREDIT CARDS

Whether he's buying dinner, shoes, or theater tickets, Chicago attorney Bob Nesbit whips out his Visa card. Nesbit uses it for more than convenience: Every time he charges a purchase, he earns frequent-flier miles on American Airlines. "I charge around \$1,500 a month," says Nesbit, "and at one mile per dollar, that comes out to about a free ticket a year."

Bank cards tied to individual frequent-flier plans have been gaining in popularity (table). Now, American Express has added a new wrinkle: Its Membership Miles program not only allows cardholders to earn travel on seven airlines, it lets them cash in miles for vacation packages.

HEY, BIG SPENDER. To determine which card deal is best for you, figure out how much you charge each month. Under the AmEx plan, mileage is redeemable only after you charge \$5,000 in one year. Infrequent card users should stick with airline cards, which credit mileage monthly for even tiny balances.

Next, compare fees and fi-



nance terms. AmEx will waive the \$25 annual fee for Membership Miles the first year, but after that, it becomes among the most expensive mileage-linked cards, at \$80 annually (including the \$55 basic fee).

Membership Miles is handy for travelers in several airline programs who want to use AmEx-earned miles to "top off" accounts to specific award levels. But if you only plan to add miles to one airline account, it may be wiser to go with that carrier's card.

Remember that some airlines place restrictions on your charging power. United put a 10,000-mile-per-month, 50,000-mile-per-year cap on credit-card mileage. Midway credits all Membership Miles you accrue but requires at least one flight before you can redeem an award.

Finally, because most mileage-linked cards charge premium interest rates of 18% and above, it's best to use them for purchases you'll pay off each month. *Jim Ellis*

HOW FLIER CARDS STACK UP

Airline	Card	Annual fee/ Interest rate	Dollar charges for free ticket
AMERICAN	Citibank Visa, MasterCard	\$50 19.80%	\$20,000
CONTINENTAL	Marine Midland MasterCard	\$45 18.95%	20,000
CONTINENTAL, DELTA, MGM GRAND, MIDWAY, NORTHWEST, PAN AM, SOUTHWEST	American Express, Optima	\$80-95 16.25%*	20,000 to 40,000
NORTHWEST	Bank One Visa	\$55 19.80%	20,000
TWA	Chase Manhattan Visa	\$75 19.80%	20,000
UNITED	First Chicago Visa, MasterCard	\$60 18.40%	20,000

*Optima only; American Express charges no interest

DATA: BW

Smart Money

A REAL ESTATE PLAY THAT WON'T GIVE YOU ULCERS

Real estate investments rarely get respect these days. Yet one group is doing very well: health care real estate investment trusts (REITs), which are publicly traded companies that invest in hospitals, nursing homes, and other health-oriented properties. In 1990, the eight health REITs averaged a total return of 21%, while REITs overall declined 15% and the stock market fell 3%. In 1991, shares of health care REITs have climbed 28%.

Why the rise? Health care is seen as a recession-proof industry: In good times or bad, people still need it. And these REITs "are not really a real estate play—they're a health care industry play," observes Rae Alperstein, an analyst with Kemper Securities Group.

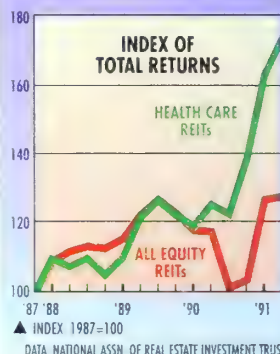
As the recent stock climb indicates, health REITs "are not a total secret anymore," says John Fosheim of Green Street Advisors, a Newport Beach (Calif.) research firm specializing in REITs. But they're still good income producers, with "prospects for steady, if not spectacular, growth," says Fosheim. Many analysts see these REITs, now yielding about 9%, returning 15% to 20% in the next 12 months.

WIDE RANGE. Health care REITs rarely finance new construction. Instead, they do buy-leasebacks—that is, they purchase an existing facility, then lease it back to the original owner. Investment strategies vary: Meditrust owns a variety of facilities, from nursing homes to substance-abuse centers to hospitals, while Nationwide Health Properties is nearly 100% nursing homes. Both approaches can be profitable as long as the REIT diversifies geographically and deals with several management

companies. Analysts advise sticking with the Big Four—Nationwide, Meditrust, American Health Properties, and Health Care Property Investors—which have averaged a total return of 37% over the past 12 months.

For investors willing to bet on a smaller company, there's Health Care REIT. Primarily invested in nursing homes and psychiatric hospitals, its stock has increased from 11 to 15 this year, and

HOW HEALTH CARE REITs HAVE PERFORMED



"I could see it at 19 a year from now," declares Donald Cassidy, a research analyst at Los Angeles broker Capital Insight. Alperstein likes Universal Health Realty Income Trust, a specialist in acute-care hospitals that has returned 52% so far this year.

Investors should keep an eye on Congress as well. Changes in medicare-reimbursement systems could hurt the profitability of these facilities. Also, health care operators themselves are now buying properties, so REITs may find it harder to get good sites, warns Robert Frank, an analyst at Alex. Brown & Sons. Still, as America gets grayer, the need for financing health care properties won't be going away. *Troy Segal*

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BusinessWeek

Leisure

CATCHING THE NEW WAVE IN WET SUITS

It wasn't quite cold enough to bring on what surfers call ice-cream headaches, but the thought of 15 mph winds and 59F water off Santa Cruz had me shivering. Yet a couple of hours later, I emerged warm, if exhausted,

burn and scrapes. At the other extreme are head-to-toe insulators for deep-water diving, such as Henderson Aquatics' \$580 semidry model equipped with a chemical pack that generates heat under water to warm your back.

Rhode Island's icy waters at such surf spots as Narragansett in January might demand the \$420 SE900 Winter Suit.

Windsurfers' arm muscles pump up as they hold the sail's boom, and the squeeze of a tight wet suit becomes tiring. BARE, Gul, Ronny, and Victory keep the upper torso and forearms fairly loose on their board sailing suits but are watertight at the ankles.

Most wet suits are made of neoprene, a synthetic rubber that runs 1 mm to 8 mm in

mile-swim time in the \$176 Tri 850 "tri-suit" from Triump Speedsuits.

Many waterskiers wear neoprene trunks, which provide warmth and padding—and don't slip off at high speeds the way simple suits can. Slalom and jump skier can get a full-length suit with rib padding.

SEAMS CRITICAL. There are new materials on the market too. One is Darlexx, which blends nylon, lycra, and a urethane film. It's lightweight, breathable yet windproof, and has some insulation. Sport Suits of Australia makes Darlexx suits that are popular in warm-water regions where it gets chilly when you dive down deep. We found them stiff and tight out of the box but they loosen up when wet.

Although wet suits go for as little as \$100, it's worth it to pay more for some features, especially good seams. The cheapest neoprene wet suits are overlock-stitched. But those seams let more water in, tear out easily, and can chafe wet skin, causing a rash. Look for a flatter stitch or better yet, a suit whose seams are stitched, glued, and then taped. The zipper should be covered with another flap to keep cold water out.

Look for tough, flexible knees: The Kraton pads O'Neill and O'Brien use gives a raves. If you're headed for really cold water, booties, gloves, and caps are a must.

While wet suits used to be uncool—and not very warm either—the new models help neophytes as well as the gnarliest dudes. *Joan Hamilton*



DRESSED FOR THE OCCASION: WRITER JOAN HAMILTON AFTER A LESSON WITH SOME SURFERS FROM O'NEILL

from a surfing lesson in the choppy soup with Jack O'Neill and son, Pat, of the water sport company O'Neill Inc. Wet suits have come a long way since the 1950s, when Jack O'Neill made his first with plastic, foam rubber, and a soldering iron. O'Neill's Animal, the \$500 model I was wearing, is one of the most advanced on the market, a black number with high-tech grooves for extra flexibility.

In our sampling of new models and styles, my colleagues and I found that there's no such thing as a standard wet suit anymore: New designs and materials allow waterwear to be tailored to specific sports, water temperatures, and proficiency levels. Body surfers can opt for inexpensive, ultralight lycra vests or suits to thwart sun-

Suits must offer warmth and freedom of movement. Some companies, such as Body Glove and O'Neill, make a wide variety, while suppliers such as Parkway focus on one sport, such as diving. Start your shopping by examining the demands of your sport and the water temperatures you typically encounter.

STAYING LOOSE. The prone-to-upright snap that surfers make to catch a wave demands a flexible suit, particularly in the shoulders, lower back, and thighs. Riders of shorter "boogie boards," who usually stay prone, don't need so much flexibility, but they need warmth. Surf East's model SE701, for about \$130, with short arms and legs, kept BUSINESS WEEK's "Boogie Bob" Barker happy in 66F water off Long Island. But

thickness. Thicker is warmer—but also more cumbersome, so most suits are 2 mm to 4 mm. The material's buoyancy is a minus for divers but a plus for triathletes, as BUSINESS WEEK's David Greising found when he shaved three minutes off his one-

Worth Noting

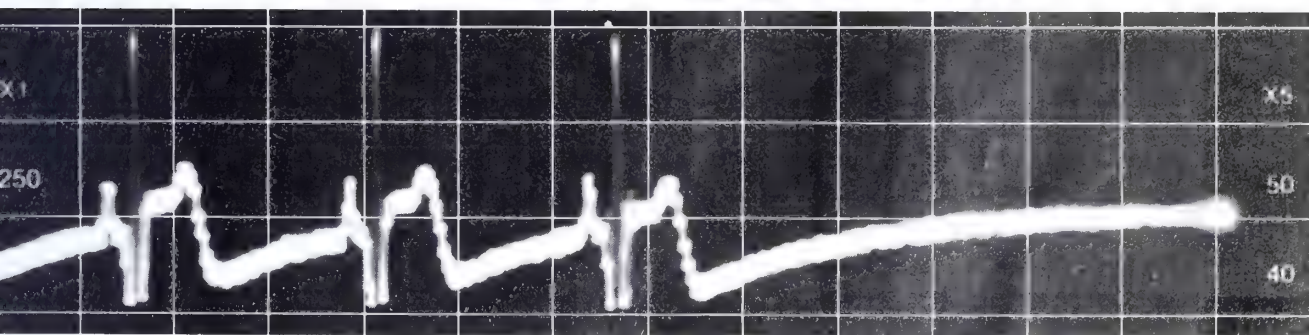
■ **TITLE ATTRACTION.** To add a professional look to camcorder movies, Creative Video Images (800 326-1387) sells a \$30 cassette of 50 animated titles for birthdays, weddings, holidays, and more. Music and sound effects are included.

■ **THE TRAIN IN SPAIN.** Beginning next April, a bullet train (187 mph) will cut in half the six-hour travel time between

Madrid and Seville. For \$1,900 round-trip, you can speed to Seville's Expo '92, then transfer to the vintage Andalusian Express for a three-day tour that takes in Córdoba and Granada. Details: 800 992-3976.

■ **NEW WATER TAX.** Owners of boats longer than 16 feet who use navigable waterways must buy a federal tax decal by July 31 to avoid a fine of up to \$5,000. The \$25 to \$100 fee can go on a credit card. Call 800 848-2100.

UNFORTUNATELY, THE WAY TO A MAN'S HEART REALLY IS THROUGH HIS STOMACH.



While your cooking was supposed to help you win someone's heart, it may also help you destroy it.

Because a diet that's too high in fat may increase the risk of heart disease as well as certain kinds of cancer.

Fortunately, you can help reduce your risk simply by eating a low-fat diet containing lots of fruits and vegetables, whole grain foods, lean meats, fish, poultry and low-fat dairy products.

For a free booklet on how to reduce the fat in your diet,

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Don't let yourself be counted among the thousands of people every year who literally eat their hearts out.

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A public service message from The Henry J. Kaiser Family Foundation

EVERYTHING
YOU NEED TO KNOW
ABOUT SCOTCH,
IN 30 SECONDS

If all you can spare is half a minute, here's all you need to know about Scotch. You have to acquire a taste for the smooth, smoky, peaty flavor. To do so, there's no better way than to acquaint yourself with a bottle of Ballantine's Finest.

That ought to do it.

Ballantine's

THE TRUE TASTE OF SCOTCH.



EVERYTHING
YOU NEED TO KNOW
ABOUT SCOTCH,
IN 15 MINUTES

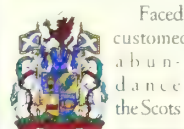
Should you have a bit more time on your hands, taste a Scotch worth savoring. Ballantine's is. First, pour yourself a glass. Then relax. Settle into that easy chair. After all, it takes time to appreciate a good Scotch. Let the ice cubes melt. That will easily take five minutes. While you're waiting, consider that Ballantine's is a smooth blend of not four, not twenty, but 42 of the finest single malt Scotch whiskies. Each chosen for its unique contribution to the overall flavor. And, perhaps, to Ballantine's number one rank in Europe. Okay. Take a sip. Taste the Highland smoke? Taste the flowery heather? Taste the earthy peat? Taste the salty sea. Mmmmmmmmm. That's what you should expect in fine Scotch. Thank you for such generous use of your time.

Ballantine's

THE TRUE TASTE OF SCOTCH

EVERYTHING
YOU NEED TO KNOW
ABOUT SCOTCH,
IN 17 YEARS

It rains a lot in Scotland. Always has. How much? Let's just say you'll never hit a sprinkler head on a Scottish golf course. The Highlands alone get more than twice the rainfall of Seattle. Even more than the Amazon River territory.



Faced with such unaccustomed natural abundance, the Scots came up with lots of things to do with water. They developed hydro power long before the industrial revolution. They boiled it to power steam engines. And they used it for transportation, building canals as early as 1761.

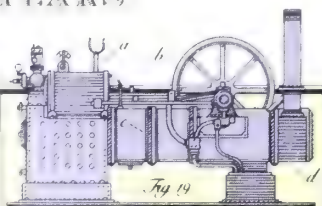
But, chiefly, the Scots dedicate their water to a more noble purpose. They use it to make Scotch whisky.

Of course it also takes peat, barley and yeast to complete the recipe, but Scotch is, after all, a liquid, and the water makes a big difference. Especially in a complex blend like Ballantine's Finest.

Some water runs from granite highlands down through peaty bogs, into small lakes, or lochs. Some runs through the peat over the granite, into streams or burns. It makes a difference, too, because Scotch made with one water has a flavor very distinct from Scotch made with another. Which is why Ballantine's has always blended different Scotches together



Balblair. A noble contributor to the blend.



Was the man who invented the steam engine inspired by a whisky still?

For smooth, mellow, yet full-bodied flavor every time, we blend mature single malts from each of the Scottish whisky regions. Some are created by our eight affiliated distilleries. Others are famous names, purchased directly from the source. (However, we bow to their desire to remain anonymous.)

In all, we use forty-two single malts to create our Finest and 12 year old blends. In the case of our noble 12 year old, none is younger than 12 years, although some are much older.



And our rare 17 year old marries an exclusive selection of more mature

spirits into a sophisticated, heady blend for the discriminating Scotch drinker. For special occasions, try Ballantine's legendary 30 year old. Only 200 cases a year find their way to the United States. That's

even fewer than the number of Rolls Royces imported each year. *We welcome all correspondence.*

Now you may well think that waiting 12 or 17 years for a Scotch is a bit excessive. And 30 years may indeed be daft. But time is on our side. We've nothing better to do. Besides, it's raining outside.



Ballantine's

THE TRUE TASTE OF SCOTCH.

Let the Poor and Hungry Feed Themselves!



For just \$100 they can.

Since 1961, ACCION International has been helping the poor and hungry feed themselves in poor urban and rural communities throughout Latin America and the Caribbean. In these desperately poor communities, we've been providing hard-working men and women with otherwise unattainable fair-rate small business loans. Without these fair-rate loans, thousands of shoemakers, bakers, artisans and street vendors would be unable to

make a living. But thanks to ACCION, people who only one year ago were barely able to keep their families alive, today have paid their loans back in full and have been given a chance to better their lives.

More importantly, they've been given back their dignity. All it takes is for you to believe in them.

For more information or to send a contribution, write to ACCION International, 1385 Cambridge St., Cambridge, MA 02139 **617-492-4930**.

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Americans with Disabilities in the New Work Force"

Its mandate:

- ◆ To introduce American business leaders to 13 million willing and able workers.
- ◆ To show why far sighted employers are seeking out workers with disabilities—*now*.
- ◆ To demonstrate how companies can obtain the competitive edge this new pool of workers provides.
- ◆ To promote the employment of persons with disabilities.
- ◆ To illuminate and support the Americans with Disabilities Act.

FROM THE PEOPLE WHO KNOW... TO THOSE WHO NEED TO

Willing and Able will open with a special introduction by Jim Brady, former press secretary to President Reagan and Vice Chairman of the National Organization on Disability.

The section, by author Kevin Hopkins, will be developed with the assistance of an involved and enlightened Advisory Board of leaders from business and government.

AN ACT OF SUPPORT THAT'S SIMPLY GOOD BUSINESS

With your advertisement in *Willing and Able*, you will tell 6.7 million readers of *Business Week's* North America edition that your company actively supports The Americans with Disabilities Act and that your company is *doing* something about it.

ADDED VALUE FOR YOUR ADVERTISING

A donation based on a percentage of the revenue generated by this special section will be made in the name of the magazine and its advertisers to the National Organization on Disability. These funds will be used directly to expand the participation of disabled persons in the work force.

- ◆ If your company has an important success

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- ◆ *Business Week* will send 10 copies each to the Human Resource Director of every *Business Week* 1000 company.
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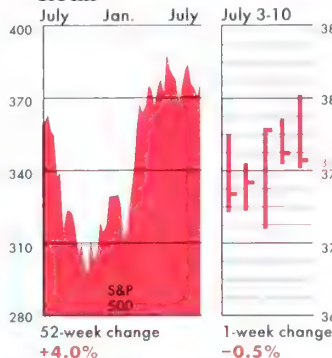
BusinessWeek

Investment Figures of the Week

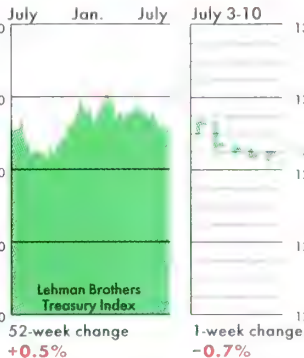
MARKET COMMENTARY

Markets sawed once again, as the market continued to trade in a narrow range, waiting to see just how strong the economic recovery will turn out to be. But while the S&P 500 stocks, as measured by the Dow Jones Industrial Average, fell for the second week, small stocks showed decent gains. Technicians are becoming bullish about the market, because it has mounted a sustained rally. The bond market remains in the doldrums, with 30-year bonds yielding 8.5%, despite new gains in commodity prices.

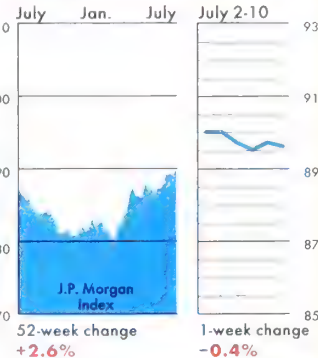
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS	Latest	Week	% change 52-week
DOW JONES INDUSTRIALS	2944.8	-0.9	0.4
DOW JONES COMPANIES (Russell 1000)	196.5	-0.2	4.6
DOW JONES COMPANIES (Russell 2000)	169.0	0.5	0.2
DOW JONES COMPANIES (Russell 3000)	208.7	-0.2	4.4

FOREIGN STOCKS	Latest	Week	% change (local currency) 52-week
DOW JONES (FINANCIAL TIMES 100)	2508.4	2.0	6.3
DOW JONES (NIKKEI INDEX)	23,121.3	-3.6	-28.4
DOW JONES (TSE COMPOSITE)	3504.2	0.3	-1.1

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.7%	5.7%	8.1%
30-YEAR TREASURY BOND YIELD	8.5%	8.4%	8.6%
S&P 500 DIVIDEND YIELD	3.3%	3.4%	3.3%
S&P 500 PRICE/EARNINGS RATIO	18.4	18.0	16.5

TECHNICAL INDICATORS

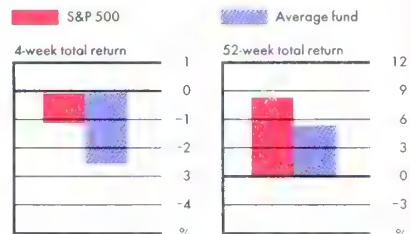
	Latest	Week ago	Reading
S&P 500 26-week moving average	368.8	366.2	Positive
Stocks above 26-week moving average	56.2%	59.8%	Neutral
Speculative sentiment: Put/call ratio	0.48	0.52	Positive
Insider sentiment: Vickers sell/buy ratio	2.96	2.73	Negative

INDUSTRY GROUPS

4-WEEK LEADERS	% change 4-week	% change 52-week	Strongest stock in group	% change 4-week	% change 52-week	Price
DIVERSIFIED CHEMICALS	5.5	22.0	ENGELHARD	12.8	40.3	30 ⁷ / ₈
COPIERS	5.5	18.6	STRIDE RITE	8.4	58.8	48 ¹ / ₄
LONG-DISTANCE TELECOMMUNICATIONS	5.4	-8.5	AT&T	7.6	2.3	39
SEMI-CONDUCTORS	4.6	8.3	CYPRUS MINERALS	17.4	-1.1	22 ³ / ₄
OVERMARKET AUTO PARTS	4.4	18.9	GENUINE PARTS	6.3	19.8	44 ⁵ / ₈
4-WEEK LAGGARDS	% change 4-week	% change 52-week	Weakest stock in group	% change 4-week	% change 52-week	Price
NATURAL GAS DISTRIBUTION	-12.5	-20.4	COLUMBIA GAS SYSTEM	-58.0	-62.1	16 ³ / ₄
COAL	-12.5	-11.4	PITSTON	-18.8	-8.2	16 ³ / ₄
OIL AND GAS DRILLING	-10.4	-25.6	ROWAN	-12.2	-27.0	8 ¹ / ₈
CONGLOMERATES	-9.4	-18.2	TENNECO	-19.8	-49.2	34 ³ / ₈
MONEY CENTER BANKS	-8.9	-2.7	FIRST CHICAGO	-16.9	-22.2	22 ³ / ₄

MUTUAL FUNDS

LEADERS		LAGGARDS	
4-week total return	%	Four-week total return	%
STRATEGIC INVESTMENTS	9.7	EQUITY STRATEGIES	-13.6
INNHAM GOLD EQUITIES INDEX	8.1	FIDELITY SELECT ENERGY SERVICE	-11.6
WINSTAY GOLD & PRECIOUS METALS	7.7	FIDELITY SELECT COMPUTERS	-11.0
4-WEEK LAGGARDS		52-WEEK LAGGARDS	
52-week total return	%	52-week total return	%
FIDELITY SELECT BIOTECHNOLOGY	46.8	BULL & BEAR SPECIAL EQUITIES	-43.8
FIDELITY SELECT HEALTH CARE	43.3	STEADMAN OCEANOGRAPHIC TECHNOLOGY	-40.8
FINANCIAL STRATEGIC HEALTH SCIENCES	42.3	UNITED SERVICES EUROPEAN EQUITY	-33.0



RELATIVE PORTFOLIOS

Amounts represent the present value of \$10,000 invested one year ago in each portfolio. Percentages indicate daily total returns.

Treasury bonds
\$10,702
-1.01%

U.S. Stocks
\$10,651
-0.48%

Money market fund
\$10,609
+0.11%

Gold
\$10,234
+0.63%

Foreign stocks
\$9,077
-2.03%

Data on this page are as of market close Wednesday, July 10, 1991, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of market close.

July 9. Mutual fund returns are of July 5. Relative portfolios are valued as of July 9. A more detailed explanation of this page is available on request.

GREENSPAN'S NEW CHALLENGE AT THE FED

President Bush has finally acted to reappoint Alan Greenspan to a second four-year term as chairman of the Federal Reserve Board. But that doesn't mitigate the unfortunate impression created by the Administration's prior delay in announcing the occupant of what is arguably the second-most-powerful position in the nation. At a time when the recovery has hardly begun, the Administration's dilatory behavior has caused uncertainty in financial markets and bred rumors that it is trying to undercut Greenspan's leadership role within the Fed and pressure him to ease monetary policy further. This is neither what the economy needs nor what Greenspan deserved.

No one can gainsay the effectiveness of the Fed's performance under Greenspan. Its quick and decisive response to the 1987 stock market crash provided succor to a badly wounded financial system and laid the groundwork for the recovery that followed. The Greenspan Fed also has brought new skill to the art of economic fine-tuning: Were it not for the Persian Gulf crisis, the Fed might well have succeeded in engineering a soft landing for the economy. Presiding over a more fractious Fed than that of his predecessor, Greenspan has been able to achieve a prudent balance between the Fed's long-term commitment to reducing inflation and the monetary needs of a growing economy.

All of these qualities and more will be needed in the months and years ahead. The integration of world financial markets, the continuing savings-and-loan debacle, and the pending reform of the banking system will continue to complicate the formulation of monetary policy. So, too, will the newfound conservative credit policies of lending institutions and the growing importance of nonbank lenders. Most of all, in an election year, the financial markets must be confident that an independent Fed will remain steadfast in its commitment to price stability and will resist political pressures to ease money unless economic conditions truly warrant such a move. One of the Greenspan Fed's greatest assets is the fact that it already has earned such confidence.

HOW TO PREVENT FUTURE BCCIs

The spectacular collapse of the Luxembourg-based Bank of Credit & Commerce International offers one clear lesson: The explosive growth of global banking requires greater coordinated international oversight.

With \$20 billion in assets, BCCI thrived as a haven for drug dealers, money launderers, and Third World strongmen by dividing its operations—and its books—among 70 countries. In so doing, it prevented any one country's regulators from gauging the scope of its worldwide activities. It wasn't until a tipster and an auditor's report revealed widespread abuses at BCCI's London offices that regulators around

the globe were finally convinced to shut the bank down.

Banking authorities in the U.S. and other leading nations have already taken steps to insure the banking system's health by setting stiff capital standards for international banks. They are also studying ways to fortify them further against swings in financial markets. But the best way to prevent another BCCI-type disaster seems to be recently proposed legislation by the Federal Reserve.

The Fed would force foreign banks to disclose more information to U.S. authorities and refuse them entry to America if they aren't subject to strict and comprehensive global oversight by their home country. It also wants authority to call for coordinated worldwide bank examinations. Such steps, if adopted here and overseas, could go a long way toward curbing BCCI-style abuse and fraud.

IT'S TIME TO REWARD REFORM IN SOUTH AFRICA

Although it was passed by Congress over a Presidential veto, the 1986 Comprehensive Anti-Apartheid Act proved to be a powerful foreign policy initiative that effectively reinforced international moral outrage at South Africa's racist practices. Under the leadership of President F. W. de Klerk, the Pretoria government has now moved faster and further toward dismantling apartheid than anyone thought possible a few short years ago.

European nations have already recognized this by lifting most of their sanctions against South Africa, with the result that many foreign companies are actively preparing for the resumption of business in that country. Since de Klerk has now met all of the conditions laid down by U.S. law, including the accelerated release of political prisoners, George Bush's decision to lift sanctions is both fair and correct.

Although South Africa's black majority has not yet secured its democratic aspirations, the process is well underway. The continuing negotiations between the African National Congress and Pretoria need the momentum that the prospect of increased economic activity can help provide. That is why the ANC itself has been courting businesses to revive investment and provide jobs.

The problem is that lifting federal sanctions against South Africa seems an empty gesture in light of the 28 states and 92 cities with similar prohibitions on their books. As long as that situation continues, companies that stopped doing business in South Africa (including McGraw-Hill Inc., publisher of *BUSINESS WEEK*) may be slow to rethink their position. Fifteen months after Namibia gained independence, for example, some cities still retain laws that discriminate against U.S. companies that do business there.

Although states and cities may regard their sanctions as leverage on Pretoria to follow through on the dismantling of apartheid in the months ahead, there is a clear risk that such laws could overstay their usefulness and actually hinder reform. If the U.S. is to retain competitiveness and advance the healing process in South Africa, state and local officials must be prepared to follow Washington in quickly scaling back sanctions as progress toward democracy continues.

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BusinessWeek

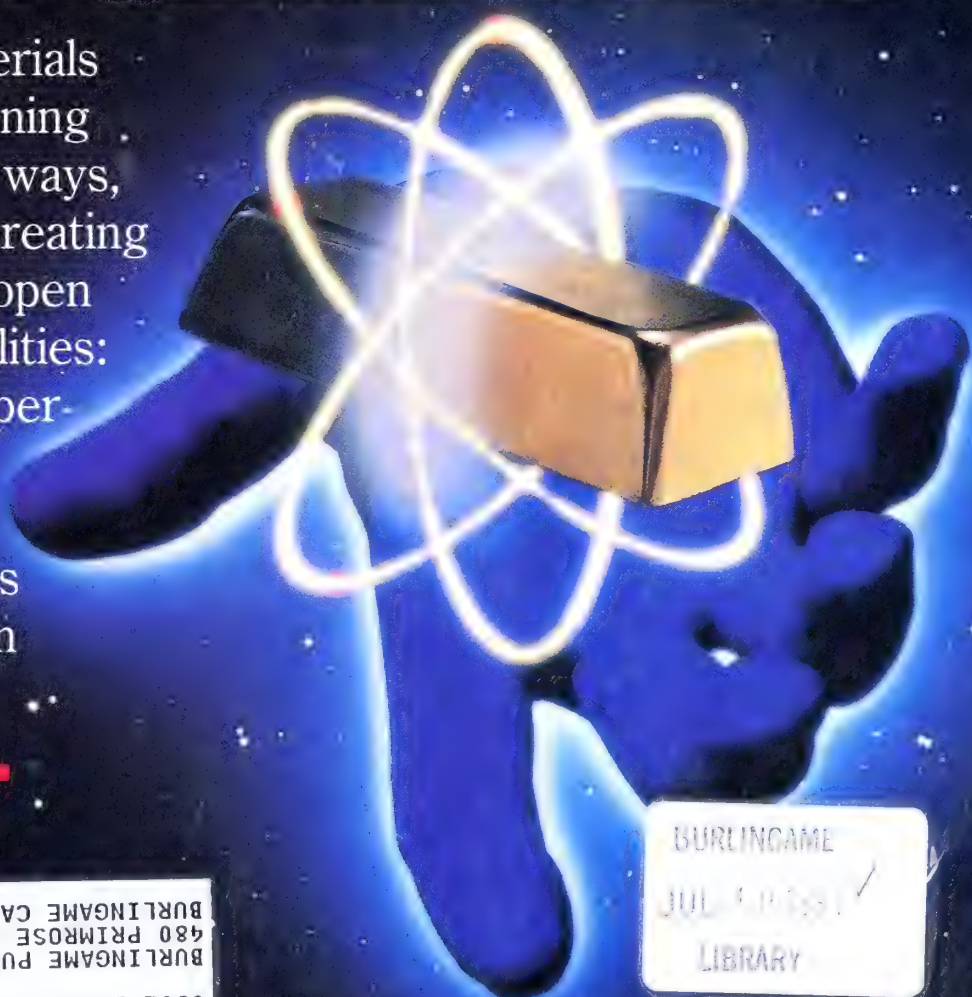


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THE NEW ALCHEMY

Call it the Materials Age. By combining atoms in novel ways, scientists are creating materials that open up bold possibilities: Pocket-size supercomputers, superlight aircraft, bridges that warn when they're weak.

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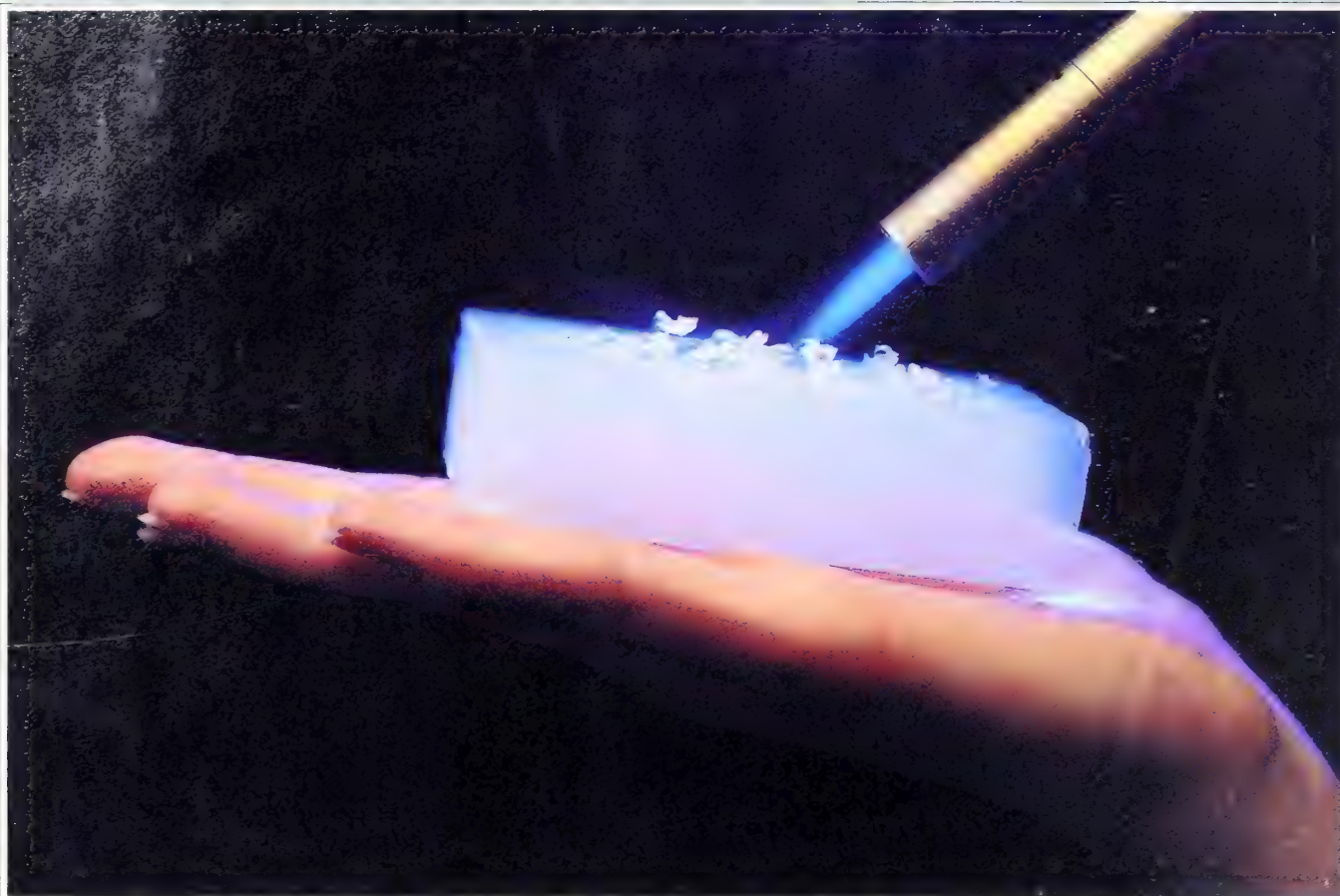
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Bob Gates is on the bench—but not out of the game

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A widespread shareholder uprising, along with SEC objections, help persuade management to scotch a 'coercive' financing plan

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A run by customers forced regulators to seize a shaky Mutual Benefit. It could happen again

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They've been pummeled ever since the stock market began its climb in late 1990

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A consultant is tied to several collapsed companies amid allegations of financial finagling

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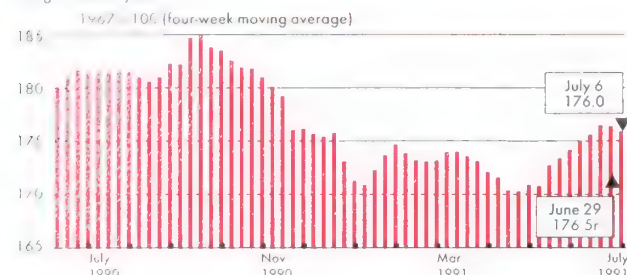
88 EDITORIALS

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BusinessWeek Index

PRODUCTION

Change from last week: -0.3%
Change from last year: -3.0%

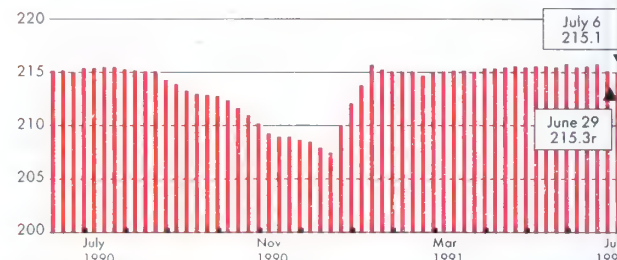


The production index declined during the week ended July 6. On a seasonally adjusted basis, output of autos, coal, and rail-freight traffic fell sharply, and truck and crude-oil refining production also decreased. Some of the decline may have been caused by plant closings for the July 4 holiday. Lumber, electric power, steel, paperboard, and paper production rose. Before calculation of the four-week moving average, the index dropped to 172.6, from 175.2.

BW production index copyright 1991 by McGraw Hill Inc.

LEADING

Change from last week: -0.1%
Change from last year: -0.2%



The leading index fell slightly for the week ended July 6, as all the available indicators moved only a little. Stock prices, long-term bond yields, and growth in M2 were virtually unchanged, while growth in real estate loans and material prices deteriorated. Data on the number of business failures were unavailable for the week. Before calculation of the four-week moving average, the index dropped to 214.1 from 214.7 in the previous week.

Leading index copyright 1991 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (7/13) thous. of net tons	1,599	1,573#	-11.9
AUTOS (7/13) units	80,601	51,690r#	10.3
TRUCKS (7/13) units	40,281	33,093r#	9.9
ELECTRIC POWER (7/13) millions of kilowatt-hours	64,778	63,304#	2.3
CRUDE-OIL REFINING (7/13) thous. of bbl./day	13,429	13,645#	-5.4
COAL (7/6) thous. of net tons	13,574#	17,004	-2.3
PAPERBOARD (7/6) thous. of tons	738.8#	764.6r	-2.4
PAPER (7/6) thous. of tons	715.0#	737.0r	0.7
LUMBER (7/6) millions of ft.	341.1#	513.0	17.8
RAIL FREIGHT (7/6) billions of ton-miles	15.3#	18.6	-6.7

Sources: American Iron & Steel Inst., Ward's Automotive Reports, Edison Electric Inst., American Petroleum Inst., Energy Dept., American Paper Inst., WWPA, SFPA, Association of American Railroads.

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (7/17)	137	139	149
GERMAN MARK (7/17)	1.79	1.82	1.64
BRITISH POUND (7/17)	1.65	1.62	1.82
FRENCH FRANC (7/17)	6.08	6.15	5.50
CANADIAN DOLLAR (7/17)	1.15	1.15	1.15
SWISS FRANC (7/17)	1.55	1.57	1.41
MEXICAN PESO (7/17)	3,016	3,012	2,873

Sources: Major New York banks. Currencies expressed in units per U. S. dollar, except for British pound expressed in dollars.

PRICES

	Latest week	Week ago	% Change year ago
GOLD (7/17) \$/troy oz.	368.900	370.900	2.6
STEEL SCRAP (7/16) #1 heavy, \$/ton	89.00	89.00	-19.5
FOODSTUFFS (7/15) index, 1967=100	197.0	194.9	-12.3
COPPER (7/13) c/lb.	104.6	106.3	-17.6
ALUMINUM (7/13) c/lb.	60.3	60.5	-17.4
WHEAT (7/13) #2 hard, \$/bu.	2.80	2.88	-10.5
COTTON (7/13) strict low middling 1-1/16 in., c/lb.	72.53	73.95	-8.1

Sources: London Wed. final setting, Chicago mkt., Commodity Research Bureau, Metals Week, Kansas City mkt., Memphis mkt.

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (7/12) S&P 500	377.40	371.75r	4
CORPORATE BOND YIELD, Aaa (7/12)	9.04%	9.04%	-2
INDUSTRIAL MATERIALS PRICES (7/12)	98.4	98.7	-2
BUSINESS FAILURES (7/5)	NA	399	N
REAL ESTATE LOANS (7/3) billions	\$403.7	\$404.0r	6
MONEY SUPPLY, M2 (7/1) billions	\$3,395.6	\$3,392.9r	3
INITIAL CLAIMS, UNEMPLOYMENT (6/29) thous.	388	423	10

Sources: Standard & Poors, Moodys, Journal of Commerce (index: 1980=100), Dun & Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. CIBC seasonally adjusts data on business failures and real estate loans.

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
INDUSTRIAL PRODUCTION (June) total index	106.9	106.2r	-2
CAPACITY UTILIZATION (June)	79.3%	79.0%r	-5
PRODUCER PRICE INDEX (June) finished goods	121.4	121.8	3
RETAIL SALES (June) billions	\$151.9	\$152.2	1

Sources: Federal Reserve Board, BLS, Census Bureau

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (7/1)	\$862.1	\$858.6	5
BANKS' BUSINESS LOANS (7/3)	308.9	308.8r	-6
FREE RESERVES (7/10)	211	974r	-57
NONFINANCIAL COMMERCIAL PAPER (7/3)	149.2	148.9	1

Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed for two-week period in millions)

MONEY MARKET RATES

	Latest week	Week ago	Year ago
FEDERAL FUNDS (7/16)	5.91%	5.82%	8.14
PRIME (7/17)	8.50	8.50	10.00
COMMERCIAL PAPER 3-MONTH (7/16)	6.03	6.14	7.94
CERTIFICATES OF DEPOSIT 3-MONTH (7/17)	5.97	6.04	8.04
EURODOLLAR 3-MONTH (7/13)	6.06	6.06	8.23

Sources: Federal Reserve Board, First Boston

#Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment
1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

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WAKE UP!

U.S. INDUSTRY IS UNDER ATTACK

In "Critical technology: A new way to say 'industrial policy'" (Top of the News, June 10), you attempt to label the Critical Technologies Act of 1991 with a textbook definition of protectionism. Does your writer forget how the U.S. semiconductor industry was driven to its knees by Japanese targeting of the industry? Textbook theory doesn't do much either for a Detroit smarting over the recent "dumping" of minivans or for the now-documented practice of Honda cars being sold in the U.S. at far below their production costs.

Listen up: U.S. industries are being targeted, and the practice continues unabated! Alarming, technologies critical to America's defense are being lost. Nearly 50% of the high-tech weaponry used in Iraq was based on U.S. technology developed in the 1970s, the production of which was lost to foreign producers in the trade wars of the 1980s. Perhaps if your writer would mix a little pragmatism with ideology, his assessment of critical technologies might not be so critical.

Representative Ralph Regula (R-Ohio)
Washington

FAMILY LEAVE: BIG TROUBLE FOR SMALL BUSINESS

I was absolutely astonished that you would favor more federal government-mandated laws, especially with a Congress that doesn't know what it is doing or what it takes to run a business ("Family leave should get the nod," Editorials, June 17).

My company, which has 86 employees, is an independent wholesale distributor that started in business in 1918. Our employee-benefit program is second to none in our industry, and we care more for our people than the government does. However, we simply can't afford to have the federal government step in and mandate our employee benefits. We just can't afford the luxury of having a key employee leave for 12 weeks. Who is going to do his or her work when we only have one person performing a

key job? What about productivity and efficiency?

Large corporations (of 500 or more employees) can handle a 12-week leave of absence because they can afford the luxury of having two employees for one position.

I am totally opposed to any more federally mandated employee benefits, and I, along with millions of small business people, will stand with President Bush on this issue.

W. Scott Smith Jr.
President
Stull Enterprises Inc.
Chadds Ford, Pa.

WHY YOU CAN'T WIN FOR LEASING

I was offered a five-year lease on a fine car recently ("Why auto companies can't win for leasing," Industries May 20). Price: \$23,000 to buy, \$350 a month to lease. The lease contract contained a variety of restrictions, penalties and other requirements—so many that probably could only drive to the local supermarket to avoid damage to the car. In addition, after three years, a mileage charge was included. Financially, the deal favored the dealer.

The \$350 a month comes to \$21,000 after five years, almost the list price of the car. After five years, I walk away with nothing—no car, nothing to trade. But the dealer has an asset—the car—which even at a conservative value of 30% of list is worth \$6,300, which he can sell again. Even if he sells it for \$5,000, he makes a tremendous profit. The lease is a sucker's game.

Daniel Feinberg
West Palm Beach, Fla.

YOU CAN'T CHANGE A COMPANY BY THROWING TANTRUMS

Your remarks should be required reading for anyone entering business ("Why big companies are so tough to change," Cover Story, June 17). I hope every chief executive officer, director, and stockholder in America saw it.

I have worked with several people who practice "management by gesture." It's a lot easier to throw furniture than

BUSINESS WEEK
JULY 29, 1991 ***3224
ISSN 0007-7135



Published weekly, except for one issue in January, by McGraw-Hill, Inc. Founder: James H. McGraw (1860-1948). Executive, Editorial, Circulation, and Advertising Offices: McGraw-Hill Building, 1221 Avenue of the Americas, New York, N.Y. 10020. Telephone (212) 512-2000 Domestic Telex 127960, International Telex 232665, Cable McGraw-Hill New York TWX 710-581-4879. U.S. subscription rate \$39.95 per year; 2 years, \$69.95; 3 years, \$94.95. Single copies, \$2. Write for rates in other countries. Business Week Subscriber Services: 1-800-635-1200.

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Readers Report

s to articulate a mission statement
t can be understood and embraced by
ryone in the company.

William M. Kennedy
Atlanta

AT REMEDIES FOR HLETE'S FOOT DON'T CURE

I like to clarify several points in your
article "Strong stuff—without a pre-
ption" (Personal Business, June 17).
Over-the-counter products for ath-
lete's foot, which contain clotrimazole,
ould be used only for the purpose indi-
ed on package labeling. Under no cir-
stances should a product such as
Lotrimin AF be used as a remedy for
aginal yeast infection.

tyne-Lotrimin and Lotrimin AF are
o separate products, which have the
e active ingredient. They require dif-
ent dosing and application. By the
y, the active ingredient in most over-
counter antifungal products would
ineffective against a vaginal yeast
ection.

Not all over-the-counter antifungals
tain the active ingredient clotrima-
e. In fact, the leading athlete's foot
ifungal—Tinactin—contains tolnaf-
e as its active ingredient. Lotrimin AF
he only major antifungal to contain
clotrimazole.

Most conditions helped by over-the-
counter products are not self-limiting. A
st infection will not be cured without
atment. The symptoms will recur,
in and again.

Douglas Petkus
Schering-Plough HealthCare Products
Liberty Corner, N. J.

FIGURE: A 40% GAIN WON'T VER A 40% LOSS

your recent article "Small is beauti-
ul—small caps, that is" (Midyear In-
ment Outlook, June 24), you make
following observation about a fund:
opping the list was Dean Witter High-
ld Securities, with a 42.41% gain [in
1] that almost exactly made up for its
small 40.1% loss in 1990." The way I
ulate it, if I had invested \$100 at the
inning of 1990 I would, as of June 7,
e \$85.30—a loss of 15%!

investors should keep in mind that
a need a higher return to make up for
loss.

Raymond Stern
San Francisco

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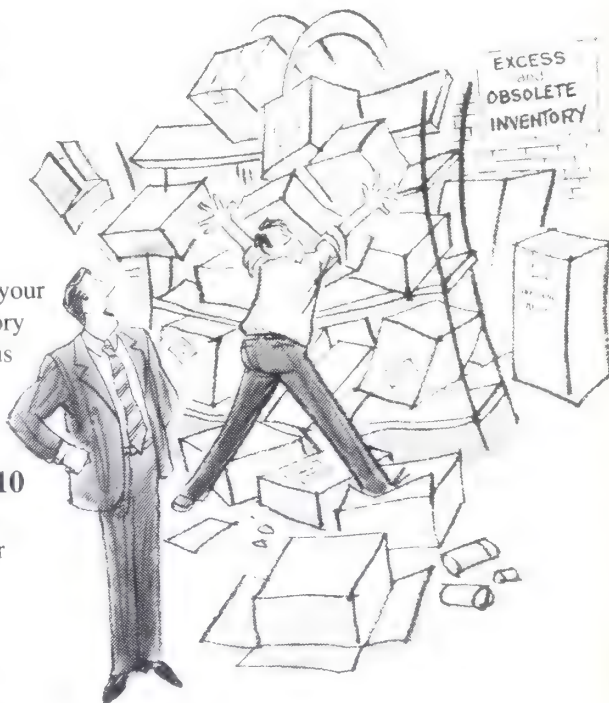
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CYBERPUNK: OUTLAWS AND HACKERS ON THE COMPUTER FRONTIER

By Katie Hafner and John Markoff
Simon & Schuster • 368pp • \$22.95

ELECTRONIC PRANKSTERS— OR AMERICA'S MOST WANTED?

One late night in 1985, a West German teenager sat down at his personal computer while his parents slept. He commanded the computer to dial into an international network that linked him with a system at a Stanford University research center. A pair of Stanford system managers detected the unauthorized user's presence, engaged him in an electronic dialogue, and ordered him to scram. Offended, the 17-year-old transmitted a virus program that kept reproducing itself until, a minute later, the overloaded Stanford system ground to a halt.

Such true tales of computer-cracking fill *Cyberpunk*, by the husband-and-wife team of *New York Times* reporter John Markoff and former *BUSINESS WEEK* staff editor Katie Hafner. Each of the book's three parts is about a wily young

man who entangles himself in a web of high-tech sin. One is Kevin Mitnick, a California computerholic who leads a bunch of overcurious kids on a decade-long hacking rampage. Another is a West German spy, Pengo, whose exploits have already been traced in a best-seller, *The Cuckoo's Egg*, by Clifford Stoll, the scientist who caught him. The last is Robert T. Morris Jr., the Cornell University grad student who cripples a national network of government and academic computers.

In each case, the hackers see themselves as harmless electronic joyriders. But often, as in the Stanford break-in, hackers swipe data or disrupt business and research. Hafner and Markoff leave it to readers to decide: Are these so-called cyberpunks merely clever pranksters? Or are they dangerous criminals?

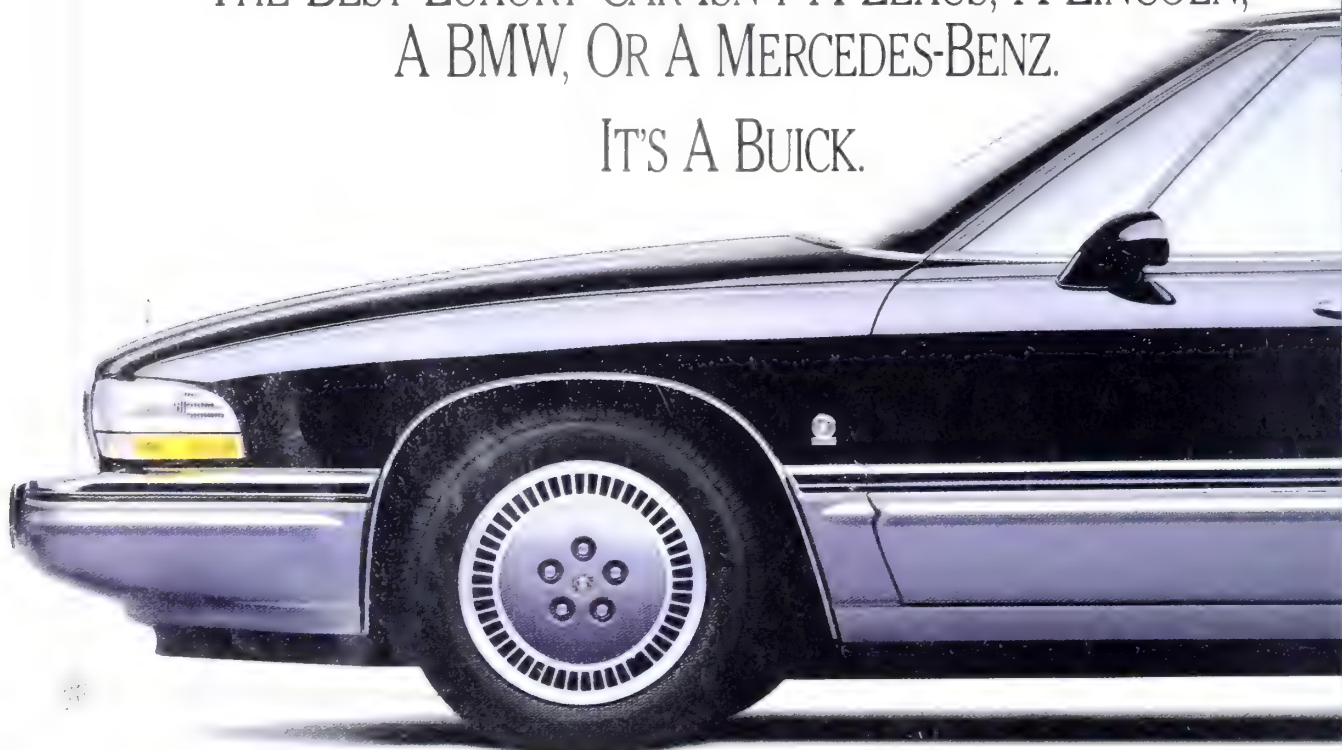
The answer isn't simple. In recent years, the media have paid enormous attention to computer crime—often exaggerating the harm done and suggesting that nerdy anarchists will soon rule the Information Age. Markoff and Hafner provide the facts that will help readers reach their own conclusions.

Sometimes the facts overwhelm. The authors' sources include court transcripts, press reports, police records, and interviews with hackers and those close to them. The result is a book crammed with details: a step-by-step rundown of each crime, a description of the computers involved, often even a note on the type of junk food the hackers were eating. At times, this level of detail grows tedious, but generally it helps bring the characters to life and helps distinguish computer-cracking from black magic.

When the book begins, in the late 1970s, the rage in the high-tech underground is "phone phreaking"—manipulating AT&T's systems to obtain free long-distance calls. A group of Los Angeles misfits band together and swap tactics for breaking into forbidden computers. Among them is a former prostitute who sleeps with men just so she can rummage through their things for con-

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THE BEST LUXURY CAR ISN'T A LEXUS, A LINCOLN,
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er access codes. Mitnick, a lonely high schooler from a broken home, emerges as the leader. Along the way, various Mitnick's sidekicks grow scared of getting caught, betray each other, lose interest. Only Mitnick persists, even though passion gets him in trouble with the law and tests his ability to hold a grudge. For the better part of a decade, he stays up late at night, lying to his wife about what he's doing while subsisting on piles of fast-food cheeseburgers. He ends up an obsessed, misanthropic blob with little regard for anything that doesn't involve a modem. While Mitnick and crew crack computers for fun and self-aggrandizement, Stoll and his band of hash-smoking hackers have other motives. A middle-class Berlin kid whose nickname comes from a video game, Pengo is paid by a Soviet KGB agent for any American software or military data he can pilfer. Readers of *The Cuckoo's Egg* will find the plot familiar. That book, however, uses Stoll as he electronically

The true stories of three wily young men who entangle themselves in a web of high-tech sin



stalks hackers from California's Lawrence Berkeley Laboratory. *Cyberpunk* follows the more intriguing action in East and West Germany.

Just about every computer jockey in *Cyberpunk* is a bit of a degenerate. Everyone, that is, except Robert T. Morris Jr. While the other hackers take drugs, lie, or run with a dangerous crowd, Morris is depicted as a shy but mischievous prodigy, whose only apparent vice is a penchant for concocting dangerous viruses and cursing when one of them

goes beyond his control.

The son of a government computer-security official, he's fond of pranks. He also once tampered with Harvard University's network so that, when users logged on, the date and other information displayed about the computer made it seem as though they'd gone back ten years in time.

With such small details, the authors enliven what might otherwise be dry, technical material. And they never lose sight of the larger issue: Should hackers be punished if they can prove they didn't intend to cause damage? The question isn't just philosophical. The Computer Fraud & Abuse Act, passed in 1986, is vague on that point. Contending there was no malice, Morris' lawyers asked the Supreme Court in June to reconsider his 1990 felony conviction. If the high court takes the case, the decision could serve as a fitting epilogue for *Cyberpunk*.

BY EVAN I. SCHWARTZ

Staff Editor Schwartz covers computer technology

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CONTROLLING THE CLIMATE THAT LET BCCI BLOOM

BY ROBERT KUTTNER



When global banks can pick their regulators, the logic of regulation is undermined. The rules should converge—and a world agency needs to supervise the supervisors

The seizure of the \$20 billion Bank of Credit & Commerce International (BCCI) invites some intriguing questions about banking regulation. The BCCI scandal underscores the mismatch between international banks and nation-bound regulators. BCCI based its operations in Luxembourg, the Netherlands Antilles, the Cayman Islands, and Abu Dhabi—not places renowned for tough banking regulation. Even nations with strong regulators, including the U.S., were asleep at the switch.

The BCCI case may be unique in the complexity of its network and the apparent extent of its fraud. But it is hardly the first case in which the ability of private bankers to move money around the globe outran the ability of national regulators to follow the paper trail. As a result of this regulatory failure, depositors—or taxpayers—will lose at least \$4 billion and maybe as much as \$15 billion.

In theory, two procedures should have ensured effective regulation of BCCI. First, under the 1975 Basel Concordat, central bankers agreed that the home country of a global bank would be responsible for supervising all of its operations. But little Luxembourg proved no match for BCCI, with its far-flung network of affiliates, subsidiaries, and laundries.

NO SHUTOUT. Second, any country where a foreign-based bank proposes to operate may shut that bank out if local authorities suspect the bank's competence or honesty. But in this case, no country did. Even the U.S. Federal Reserve was gulled, with an assist from power-lawyer Clark M. Clifford, into approving BCCI's acquisitions in the U.S. despite the Fed's misgivings about the parent bank. It was the Bank of England, not the Federal Reserve, that belatedly launched a major investigation of what now appears to be not just fast-and-loose banking but massive fraud.

The ability of global banks to seek out the weakest regulatory forum is not unlike the situation in the U.S., where banks are able to select the most accommodating state or federal regulatory environment. Allowing banks to pick their regulator, on whatever scale, undermines the logic of regulation. If Luxembourg is not up to the regulatory job, it should not be a designated regulator for global banks.

What's required is much tighter international collaboration, as well as a convergence of regulatory standards. Each nation's bank regulation is vulnerable to national political pressures. But central bankers, acting in concert, can keep one another honest. Some international agency, perhaps the Bank for International Settlements (BIS), which is sometimes called the central bankers' central

bank, needs to supervise the supervisors. There is no legitimate reason for a major international bank to operate from obscure islands, other than to avoid taxes or regulation. Moreover, closely held private banks such as BCCI, which are not subject to scrutiny under securities laws, should not be allowed to acquire retail banks freely and control them.

The underlying problem is that commerce today is international while regulation is national, and regulation itself is out of fashion. A chain of de facto cooperation among central bankers is only as strong as its weakest link. The major central banks reluctantly acknowledged this problem, first in the 1975 Basel Concordat and again in 1988, when they agreed on a common minimum standard of bank capital equal to 8% of bank assets, which becomes effective in 1992.

Nations are reluctant to share or to delegate national sovereignty, especially on something as basic as banking regulation. But, of course, national sovereignty has already been ceded—to private international bankers who can outrun national laws. In international banking, the U.S. and Britain, the traditional stewards of global finance, are usually the regulatory hawks. Japan and Germany, in contrast, have tended to view the strength of their own banks as a source of competitive advantage and have cared less about the international banking system as a whole. Moreover, coming from corporatist societies, in which tight Establishment of senior bankers, government officials, and business leaders—rather than a rule book—attends to the solvency of banks, the Germans in particular have felt little need for a new legalistic global schema.

WICKED LEFT-RIGHT. Ironically, however, it is in legalistic America where bank regulation has lately become degraded. Under the Reagan and Bush Administrations—with a nice bipartisan assist from such Democrats as Clark Clifford and California Senator Alan Cranston—the U.S. has failed to police its own banks, let alone the branches of foreign ones. America, with its lethal brew of Republican ideology and Democratic opportunism, is no role model of bank supervision.

Indeed, if the Bank for International Settlements had been empowered to toughen up lax regulatory environments, it should have placed the U.S. on the same list with Luxembourg, the Netherlands Antilles, and the Caymans as nations not competent to regulate large global banks. We need greater internationalization of bank supervision not just to keep shady bankers from falling between the national regulatory cracks, but to put some spine in America's own feeble stewardship.

ROBERT KUTTNER IS ECONOMICS CORRESPONDENT FOR THE NEW REPUBLIC AND AUTHOR OF THE END OF LAISSEZ-FAIRE

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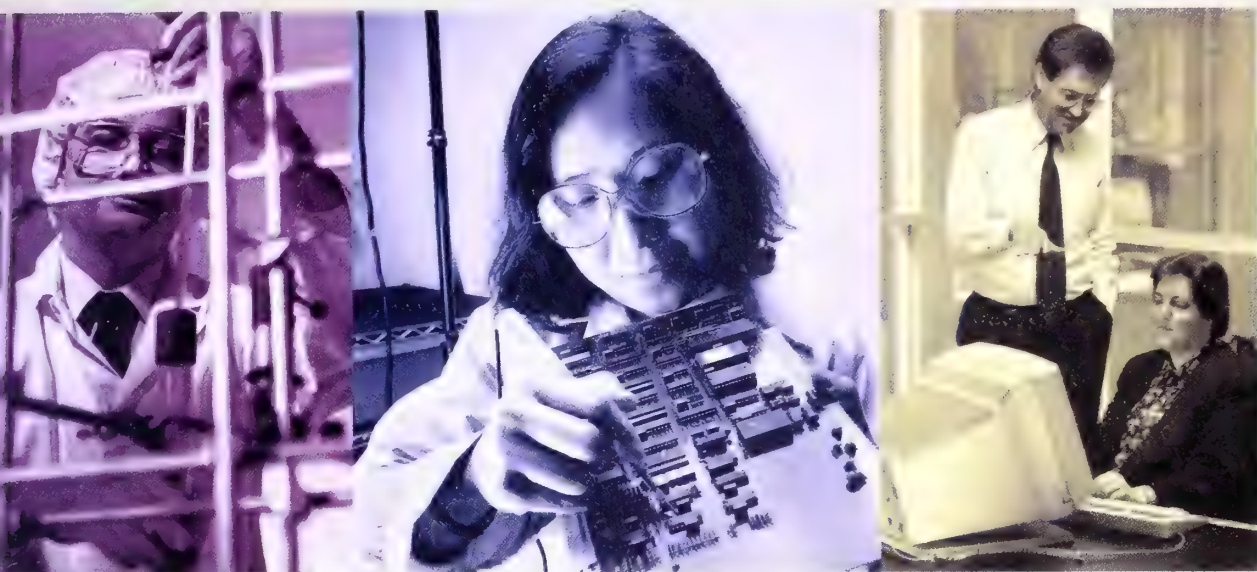


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*William Schaeff
Director of Information Services
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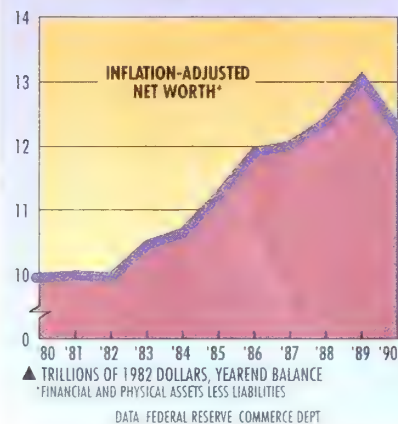
THE OPEN ADVANTAGE.

BY KATHLEEN MADIGAN

EVEN WITH LESS, CONSUMERS MAY SPEND MORE

The drop in the stock market and the collapse in home prices put a crimp in personal wealth last year. In fact, real household net worth—assets minus liabilities—dropped by 5.8% in 1990 (chart), the biggest decline since the Federal Reserve started keeping records in the early 1950s. The wealth slump has raised worries that ailing consumer spending will decline further as households divert income away from shopping malls and shift it toward savings

HOUSEHOLD WEALTH TAKES A BIG PLUNGE



accounts in an attempt to rebuild their depleted assets.

That's not likely to happen, says economist Giulio Martini of securities firm Sanford C. Bernstein & Co., who took a look at the data on the "wealth effect." This economic idea holds that as household balance sheets get fatter, people spend more, and as they get skimpier, people cut back. Martini concedes that over the past 45 years, it appears that wealth and spending have moved in lockstep. Nevertheless, he argues that spending isn't dependent on wealth but rather "both are dependent on the same things—the strength of GNP, monetary policy, and the behavior of inflation." Indeed, wealth has fallen in nine years during the postwar era. But consumer spending for those years slowed only slightly. It grew an average of 2.1% in those years, compared with its long-term trend of 3.3%. And in the years following a decline in wealth, Martini found that consumer spending bounced back smartly, rising an average of 3%.

Martini also notes that wealth in the

U.S. is highly concentrated among a small segment of the population. When the rich take a hit in their portfolios, they still have other resources to maintain their spending pace. That's why the stock market crash of 1987 had little effect on the overall economy, he says.

"Today's problem in housing has more potential to cut spending," Martini admits. But he points out that most people sell their homes to trade up to another house. So while they may not get as much as they would like for their old residence, they benefit from the downward shift in the price of their next home. "The winners offset the losers," concludes Martini, "so home prices don't really affect economic growth."

With his forecast for a strong second-half recovery and lower inflation, Martini estimates that despite the plunge in wealth, real consumer spending will grow at a healthy 3.5% this year.

HEY, ROGER CLEMENS, EAT YOUR HEART OUT

How much would Babe Ruth be paid in today's baseball market? What about Lou Gehrig or Cy Young? Such questions have started many a barroom brawl. But a team of economists at the University of Dayton, Ohio, has come up with a way to estimate how much the boys of summers past would be earning if they were on the field in 1991.

Economists Lawrence H. Hadley and Elizabeth F. Gustafson and researcher Mary Jo Thierry discovered that about 30 factors determine salaries in the major leagues. High on the list are, of course, such stats as batting averages or strikeouts. But also important are free agency and arbitration—bargaining chips not available to players before the late 1970s. In addition, the economists factored in such significant variables as the team's win-loss record, its city, the player's years in the league, and his position. They also found that, on average, a hitter's salary peaks in his 13th year of play, while a pitcher's income tops out in his 11th season.

By using a computer model of the relevant stats, Hadley and his team have calculated the salaries for 150 of baseball's greatest hitters and 100 of the greatest pitchers as if they were now at the peak of their earning potential and had negotiated their contracts in 1991. The big winner: the New York Yankees' Lou Gehrig, who would be raking in \$7.8 million. The highest-paid pitcher is Washington Senator Walter Johnson, who would earn a cool \$7.5 million, fol-

lowed by Cy Young, with \$7.1 million.

Hadley points out that inflation has little to do with predicted salaries. For example, Babe Ruth's 1930 salary of \$80,000 would equal about \$725,000 today's dollars. But the Babe would have made \$7.5 million if his baseball skills were on the block today. That puts him second on the hitters' list.

The rankings aren't designed to determine who is the greatest baseball player of all time, Hadley cautions. "What this does is compare the economic value of players on the basis of their career performance," Hadley adds. "The changing nature of baseball—from the use of AstroTurf to the emergence of specialized players such as the designated hitter—might mean that stats like Gehrig would play less today and would accumulate less impressive statistics. Even so, the predicted-salary data give fans a new way to compare players. And the game's numbers freaks get what they crave: another statistic."

PAY HIKES VS. INFLATION: A SURPRISE WINNER

Good news for workers at last: According to the Conference Board survey of 537 private companies, salary increases will surpass the inflation rate for the first time in four years. The survey finds that pay hikes will average 5% this year and next. That's better than the expected increases in prices of 4.7% in 1991 and just 3.8% in 1992.

NOW CONSTRUCTION IS SINGING THE STATEHOUSE BLUES

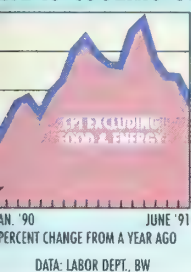
As if the construction industry hadn't enough troubles: the credit crunch, soft home prices, and the oversupply of commercial real estate. Now add on more: the budget crises at state and local governments.

Nancy Lazar of International Strategy & Investment Group Inc. points out that public spending has become very important to the building industry. State and local governments' share of total construction spending has risen sharply from less than 17% in 1984 to nearly 24% in 1991. But budget problems across the country are sure to mean cuts in appropriations for highway and sewer projects. Lazar projects real government outlays for construction will drop 5% this year, contributing to a decline of at least 10% in all building activity.

THE ECONOMY IS LOOKING STRONGER —NO THANKS TO WASHINGTON

In many ways, the U.S. economy is bouncing back from the 1990-91 recession along classic lines. Consumers are spending again. Businesses, after slashing their inventories during the downturn, are now fighting with their stockpiles down. So companies are boosting production in order to catch up. It's a recovery process that has unfolded throughout the postwar era. But this time, there's one important difference. The outlook for demand—particularly by consumers—is on unusually shaky ground. Clearly, the often-recited litany of interrelated structural problems stemming from heavy debts, overvalued real estate, and weak banks, all weigh on demand. But right now, the biggest obstacle to demand growth is economic policy.

INFLATION'S CORE RATE IS COOLING OFF



en especially stingy with money growth. The latest data show that the downdraft from tight money will not block the classic dynamics of recovery. Without the traditional stimulus from government to help sustain the process, especially in the face of so many untraditional drags on demand, the upturn could start to sputter before the year is out.

FACTORIES ARE REALLY STARTING TO HUM

For now, most of the numbers support the upbeat assessment of the economy delivered by Fed chairman Alan Greenspan in his semiannual report to Congress on July 16. He proclaimed that the recession was over and that the outlook for inflation was improving. Indeed, the consumer price index rose a modest 0.2% in June, down from 0.3% in May. The core CPI, which excludes food and energy, rose a faster 0.4% in June, but the yearly pace of core inflation fell to 5%, from 5.7% in February (chart).

The key housing and auto sectors continue to firm up. Sales of domestically made cars, which had risen from an annual rate of 6.1 million in May to 6.7 million in June, began July at a 7.3 million pace. And housing starts rose 5.7% in June, to an annual rate of 1.04 mil-

lion, as all four regions of the country posted increases. Both housing starts and permits to begin new construction rose for the third consecutive month.

That partly explains why the factory sector is looking almost vibrant. Industrial production rose 0.7% in June, the third consecutive gain. Output of cars and trucks, goods for the home, construction supplies, and a broad array of materials posted big gains.

In addition, increases in both April and May were revised 0.2 percentage points higher than first reported. The May rise now goes into the books as 0.7%, and the April increase gets logged in at 0.5%. That makes the strongest three-month advance in nearly four years. The quarterly pace of output rose into plus territory for the first time since the third quarter of last year (chart).

Industry also used more of its production capacity in June. The industrial operating rate rose to 79.3% from 79% in May. However, that is below the 82% level that raises concerns about bottlenecks and price pressures. The producer price index for finished goods fell 0.3% in June, the core PPI was flat, and no cost pressures are brewing at the earlier stages of processing.

Low inventories—in the face of rising sales—are playing a big role in the recent production gains. Businesses kept their stockpiles very lean during the recession. They started to pare them down last July. However, businesses apparently got caught short in the spring as rising sales accelerated the liquidation (chart).

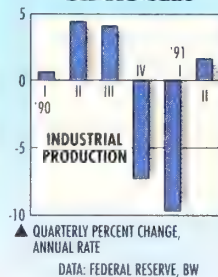
Inventories held by manufacturers, wholesalers, and retailers fell 0.5% in May, following declines of 0.3% in April and 1% in March. Since March, business sales have jumped 2.5%. The combination of falling inventories and rising production strongly suggests that the inventory-cutting in recent months has been involuntary, meaning that businesses will have to gear up output until stockpiles are back to desired levels.

MONEY IS ON A SHORT LEASH

Demand is what keeps the recovery process going, though, and that's where policy will be hurting more than helping. In the past, for example, a sharp pickup in money growth has always powered an economic recovery. But this time, no such fuel is in sight.

Although the Fed began to ease monetary policy aggressively last December by knocking down short-term

OUTPUT GETS BACK ON ITS FEET



Business Outlook

interest rates, the yearly growth of inflation-adjusted M2 remains in the downtrend that began four years ago. In fact, real M2 is still falling from its year-ago level.

That means spending by consumers and businesses is being constrained by a lack of liquidity. In Greenspan's own words on July 16, the relationship between M2 and the economy is "one of the most enduring in the financial system." Without faster money growth, the recovery in domestic demand will look pale by postwar standards.

Fiscal policy is also a big restraint. The White House's latest estimates put the federal budget deficit for the 1992 fiscal year at a staggering \$348 billion, up from \$282.2 billion expected for 1991, and \$220.5 billion in 1990. In the past, such a widening in the deficit would provide a stimulus to the economy. That's not true this time.

Almost all of the growth in the deficit from 1990 to 1991 can be traced to funds needed for the bailout of the S&Ls. That's simply a shift of debt from the private sector to the public sector with no impact on economic growth. And that's true for much, if not all, of the deficit increase from 1991 to 1992.

In addition, the impact of higher taxes, spending cuts, and payroll reductions at the state and local levels has not yet hit the economy. That will show up in the second half, since July marked the beginning of the new fiscal year for most state and local governments.

SHOPPERS MAY STAY HOME THIS SUMMER

Most of this policy constraint will fall back on consumers, a sector where the fundamentals of demand are already pretty wobbly. Heavy debts, low savings, and meager growth in incomes pretty much sum up the problem. In addition, it's still not clear if the spring

pickup in consumer spending is sustainable or if it was simply a burst of pent-up demand that consumers had harbored during the Persian Gulf war.

Even with the June increase in car buying, retail sales fell 0.2% last month. Excluding cars, retail receipts dropped 0.5%. Sales of home-related durable goods declined sharply. Department store receipts also fell, as did sales in clothing stores. That supports the notion that May's summer-like weather stole some sales of hot weather items from June and July.

Moreover, the rise in car sales has been helped by new leasing programs. During the past six months, auto leasing has surged nearly 30%, as dealers have offered attractive incentives and extended the leasing option to lower-priced cars. As in the past, though, such programs could be borrowing sales from future months.

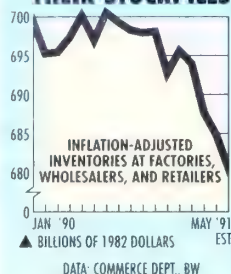
Adjusted for inflation, retail sales have not shown any upward movement since February (chart). All of the recent rebound in sales occurred in February, after victory in the Gulf seemed assured.

Since spending began the second quarter on a higher plane, the quarterly average of real retail sales was above that for the first quarter, which gave a

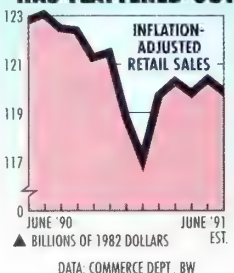
boost to last quarter's real gross national product. But the flat pattern of sales through the spring does not bode well for consumer spending in the third quarter.

The latest forecasts by the Fed and by the Administration call for growth in real GNP of about 1% between the fourth quarters of 1990 and 1991. That implies growth of about 3% during the second half of the year. That is certainly a respectable pace, but there is a growing risk that Washington's forecast will be done in by its own economic policies.

BUSINESSES SLASH THEIR STOCKPILES



RETAIL VOLUME HAS FLATTENED OUT



THE WEEK AHEAD

FEDERAL BUDGET

Monday, July 22, 2 p.m.

The U.S. Treasury is expected to report a \$4 billion deficit in June, according to economists surveyed by MMS International, a division of McGraw-Hill Inc. That would be an improvement from last June's \$11.1 billion gap, but more red ink is on the way. The White House has announced that the deficit for fiscal 1991, which will end on Sept. 30, will total record \$282.2 billion. And 1992's budget will be \$348.3 billion in the red. The large increase for next year is partly the result of delays in bailing out failing thrifts and banks. The postponement will shift the government's costs from this year into 1992. The budget

office also revised downward its projections for tax receipts next year, although it is forecasting a relatively healthy 3.6% rise in the real gross national product next year.

DURABLE GOODS ORDERS

Wednesday, July 24, 8:30 a.m.

The MMS economists expect that new orders placed at durable-goods manufacturers rose by about 1% in June. That would be the third increase in a row, including a 3.4% rise in May. The strong 0.7% rise in factory output for June suggests that demand has picked up. The upward trend in new orders is likely to boost the backlog of unfilled orders, which has not increased since last year. Excluding the booming aircraft industry,

unfilled orders are down by a steep 6.1% from a year ago.

GROSS NATIONAL PRODUCT

Friday, July 26, 8:30 a.m.

The economy probably grew at an annual rate of 1% in the second quarter, says the MMS report. That follows a decrease of 2.8% in real GNP in the first quarter. Growth in consumer spending and homebuilding and an improvement in foreign trade likely offset declines in business outlays for plants and equipment and further drawdowns in nonfarm inventories. Economists also project that the GNP price deflator rose at an annual rate of about 3.4% last quarter. That's a sharp improvement from the inflation measure's rise of 5.2% in the first period.

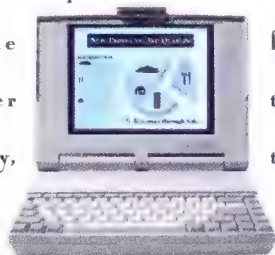
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CHEMICAL-MANNY HANNY IS A GLIMPSE OF THE FUTURE

For the past decade, Manufacturers Hanover Corp. Chairman John F. McGillicuddy and Chemical Banking Corp. Chairman Walter V. Shipley have been staring at each other from their headquarters offices on either side of Park Avenue. Rivals in New York's rough-and-tumble banking business, "we used to communicate by sign language," jokes McGillicuddy, gesturing with one of his ever-present cigars.

They still are—but the only sign they're using now is a high-five. On July 15, McGillicuddy and Shipley stepped before a phalanx of TV cameras to confirm

months of Wall Street rumors. By year-end, the chairmen said, the banks will merge into a \$135 billion powerhouse that will be second in size only to Citicorp in the U.S. (table, page 27).

That alone, says McGillicuddy, sends a "powerful message" to banks nationwide: Suddenly, the leisurely restructuring of American banking has slammed into high gear. With two of the nation's biggest money-center banks taking the plunge, bankers from the Hudson to the Golden Gate are getting moving on their own merger plans before someone else gobbles them up (table). "There have been discussions among everybody," says Christopher T. Mahoney, associate director of Moody's Investors Service Inc.'s Financial Institutions Group.

"There will be a domino effect." Many regulators, analysts, and bankers think that's long overdue. Despite a wave of mergers among money-center banks more than 30 years ago and the more recent emergence of such powerful "superregional" lenders as NCNB Corp. and Banc One Corp., the U.S. banking system remains weighed down by thousands of costly branches and handicapped by a shortage of capital. That has left too many big and small banks poorly fortified against bad real estate, takeover, and Third World loans, and ill-equipped to profit from the new businesses the Bush Administration would like to see them enter.

BIGGER AND FEWER. Worse yet, weakened U.S. banks have all but disappeared from the global scene. In a world market increasingly dominated by rich Japanese and European megabanks with as much as \$400 billion in assets apiece, even the once-dominant Citi, with just half that amount, long has been in re-

The merger
sends a
'powerful
message'

JOHN F. MCGILlicuddy
Manufacturers Hanover



t (page 26). But now, a combination forces is spurring the banking industry's turnaround effort. The White House and Federal Reserve are pushing hard to shrink the number of the nation's 12,000-odd banks. What's more, the climate for pulling that off is brightening dramatically. With the economy improving, bank stocks have soared as much as 50% this year (page 27), giving larger banks a greater ability to raise capital or buy competitors. Chemical, for example, is swapping 1.14 of its common shares for each of Manny Hanny's.

Each strength will go a long way toward helping to reshape the industry as a series of banking fortresses built on the Chemical-Manny Hanny model. Dominant in their local or regional markets, they'll try to cut costs ruthlessly and generate enough profit to finance future expansion into new regions and product lines. As early as the mid-1990s, figures from Merrill Lynch, L. Bryn Mawr and McKinsey & Co., the core U.S. banking group, predict the number of banks could be down to 7,000 from 15,000 such banks today. Perhaps 100 or two smaller ones, from 125 holding com-

panies today. While some lawmakers, including Senate Banking Committee Chairman Donald W. Riegle (D-Mich.), want to limit the size of such megabanks, that may only forestall the inevitable. "You're going to see \$250 billion banks and even larger," Bryan insists.

CROWDED PIPELINE. Undoubtedly, bankers are thinking more along these lines than ever. Coincidentally or not, the Chemical-Manny Hanny announcement was just hours old when news about other local or regional deals began to break. First came Cleveland's \$11 billion Ameritrust Corp., which abruptly ended two months of stonewalling and agreed to talks on a \$900 million bid by hometown rival National City Corp. Then C&S/Sovran Corp. Chairman Bennett A.

Brown, who previously had been cool to a \$3.8 billion offer from NCNB Chairman Hugh L.

McColl, suddenly agreed with his board to talk terms, including price.

"There's a certain inevitability" that other deals will follow, says Fed Governor Edward W. Kelly Jr. Analysts say that the Chemical merger will put pressure on other New York mon-



The friendly rivals 'came together by divine guidance'

WALTER V. SHIPLEY
Chemical Banking

HOW DOMESTIC BANKS COULD LINK UP...

AMERITRUST Cleveland
National City wants it. Banc One or NBD Bancorp might make counteroffers

BANK OF NEW YORK New York
Chase Manhattan is mulling tieup, but Bank of New York may have other plans



C&S/SOVRA Norfolk
NCNB is bidding \$3.8 billion to build a Southern superregional

SECURITY PACIFIC Los Angeles
May resume aborted merger talks with Wells Fargo. First Interstate Bancorp looms as a dark horse



SHAWMUT NATIONAL Hartford
Bank of Boston is interested. BankAmerica, too, perhaps

SOUTHEAST BANKING Miami
First Union or Barnett Banks may want to make a deal

...AND POSSIBLE BUYERS FROM ABROAD

BANK OF MONTREAL Canada
Now owns Chicago's Harris Trust, may zero in on Continental Illinois. But First Chicago may be eyeing Conti, too

CREDIT LYONNAIS France
Already an aggressive lender in the U.S., wants even more growth



WESTPAC BANKING Australia
Looking for U.S. buys to add to \$85 billion in assets Down Under

DATA BW

DON'T EXPECT CITICORP TO PLAY COPYCAT

The anxiety level at Citicorp just jumped. But don't look for the nation's largest banking company to leap into a merger. Citi Chairman John S. Reed and crew are still busily tidying up yesterday's messes: loans to the Third World, real estate developers, and buyout artists among them. "Citi's only reaction now has got to be to clean up its balance sheet," says James J. McDermott Jr., banking analyst at Keefe, Bruyette & Woods Inc. "There's very little they can do on the expansion front until their capital ratios are stronger."

Citi's second-quarter results, announced a day after the Chemical-Manufacturers deal was unveiled, didn't offer much immediate hope. The bank reported a 3¢-per-share loss, vs. a 6¢-a-share profit last year, and common equity as a percent of total assets slipped a notch, to 3.7%.

About the best news in Citi's earnings report was that costs edged down 4%. One reason: Citi shrank its payroll by 5,000, to 90,000. Still, that's an unhappy reality for a bank that for so long grew by snatching away business. "Their challenge is to generate real revenue growth," says Salomon Brothers Inc. bank analyst Thomas H. Hanley.

'VERY AGGRESSIVE.' "We have a ways to go," says Reed. To do that, says Citi Executive Vice-President Thomas E. Jones, the bank is "absolutely committed to building core franchises." And so maintaining an edge in the New York market, where the merged Chemical Banking Corp. and Manufacturers Hanover Corp. will take the lead in deposits, is a top priority. New Yorkers can look forward to a marketing blitz from Citi. "We intend to be very aggressive," says Pamela P. Flaherty, a Citi consumer banking executive.

The importance of Citi's consumer banking operation can hardly be overestimated. "The consumer bank is the one cylinder of the engine that has been firing consistently over the past

three to five years, but it is showing signs of getting tired," says Donald McNeese, head of the financial institutions practice at Cresap/Towers Perrin's New York office. Credit cards, where one analyst estimates the consumer division gets 70% of its earnings, face increasingly stiff competition. Yet McDermott says it "will improve its prospects once economic conditions in the U.S. improve."

While Citi circles its wagons in New York, Reed says problems are growing out West. As growth in sour real estate loans in the Northeast begins to slow, some think California is about to see a surge in bum assets. As of Mar. 31, Citi had almost \$4.2 billion in real estate loans in the West, much of them in California, and about a third of Citi's total real estate loan portfolio.

Even once Citi gets beyond some of these problems, it's far from clear that it's in for a big merger. "It's hard for me to imagine Citi merging with anybody because of the intensely separatist culture Citi has maintained," says

Richard L. Huber, vice-chairman of Chicago's Continental Bank Corp.

A bigger deterrent may be Citi's capital constraints. It has been raising capital by selling assets, such as 50.3% of its insurance subsidiary, AMBAC—which Citi is due to close on shortly—and by selling stock. The stock sale annoyed investors, whose holdings could be diluted. Worse, asset sales may hurt Citi's ability to boost capital internally when Reed concedes operations aren't yielding enough capital.

In time, Citi can come back. "If they address their real estate and [Third World loan] problems, which I think they are, they have the capacity to make a lot more money than Chemical and Manufacturers Hanover combined," says Mark Gross, senior vice-president at IBCA Inc. But first, Reed has lots of sweeping up to do.

By Suzanne Woolley in New York



EVEN IF REED WANTS TO MERGE, HE NEEDS CAPITAL

ey-center banks to fortify their position fast. Industry sources say Republic New York Corp., a well-capitalized \$30 billion lender that already has acquired two local savings banks, is shopping for more. And many expect Chase Manhattan Corp. and Bank of New York Co. to merge to cut expenses.

But some say Bank of New York, which slashed overhead 20% after merging with Irving Bank Corp. in 1988, may have other plans, perhaps including a takeover in Florida. Indeed, if Congress approves the Administration's restructuring plan, some analysts think Chase or Citi may become the first big bank to link up with industrial companies.

MENAGE A TROIS? If takeover talk is rattling New York, it's jolting Chicago, where a handful of banks are nervously eyeing one another. Hot on the heels of the Chemical deal, Holland's \$90 billion ABN-AMRO Holdings, which already owns Chicago's La Salle National Bank, followed with a \$430 million takeover of Illinois' largest thrift, Talman Home Federal Savings & Loan Assn. Now some senior bankers are talking of a superbank combining Continental Bank, First Chicago, and Northern Trust.

If this *ménage à trois* doesn't come to pass, perhaps a wealthy Canadian or German giant might pick off one or two. "I can't say that we're sitting pretty," says Continental Vice-Chairman Richard L. Huber. "Anyone who says that today is in danger of being made a fool."

California, too, is buzzing with merger talk. Investment bankers and analysts began speculating that the on-again-off-again negotiations between Wells Fargo & Co. and Security Pacific Corp., with \$141 billion in assets between them, will finally bear fruit. If they don't, one well-connected California investment banker says, each bank soon may seek out other partners. Says Shipley: "There's a lot of room [for further consolidation]. There's room in New York. There's room in Texas. There's room in the Southeast."

Of course, takeovers don't always work the way they're intended. The granddaddy of superregionals, Bank of New England Corp., crashed last January after its regional expansion fell victim to staggering real estate losses. Chemical itself piled up huge losses on acquisitions in Texas and New Jersey.

But things will be different this time, according to McGillicuddy, 60, who will run the new bank, and Shipley, 55, who will become CEO in 1994. They say that by merging in one market, they will be able to shrink costs. The new Chemical—which will drop the 138-year-old Manufacturers name—will slash the combined banks' payroll by 6,200, close 70 branches, and reduce overhead by

million a year. ng so is vital, only to offset weight of the joined institutions' billion in sour estate, leveraged out, and Third ld loans. "This is endous news," one Chemical ex- ive. "It means the t will survive. I hope I can hang on my job."

things go as ned, Chemical will rge with one of industry's largest of gilt-edged cli- including United

anologies Corp. and RJR Nabisco ings Group Inc. It will also boast med-down global desks trading ls, currencies, options, and swaps. new bank will claim \$88 billion in sits and a full 40% of the cash in York's five leading banks. And its branches in New Jersey and us, it will become one of the nation's enders to the lucrative "middle mar- of midsize businesses. "We'll be er and stronger," says McGilli-

CHEMICAL WOULD BE NO. 2 IN THE U.S....

Company	Total assets* Millions
1 CITICORP	\$216,914
2 CHEMICAL BANKING	135,459**
3 BANKAMERICA	111,934
4 CHASE MANHATTAN	98,089
5 J.P. MORGAN	98,835
6 SECURITY PACIFIC	83,096
7 NCNB	66,005
8 BANKERS TRUST NEW YORK	57,350
9 WELLS FARGO	55,691
10 FIRST INTERSTATE BANCORP.	50,402

*As of Mar. 31

**Pro forma

DATA: IBCA LTD.

...BUT JUST A DISTANT ALSO-RAN GLOBALLY

Company	Total assets* Millions
1 DAI-ICHI KANGYO BANK	\$409,076
2 MITSUI TAIYO KOBE BANK	403,391
3 SUMITOMO BANK	394,642
4 MITSUBISHI BANK	379,735
5 FUJI BANK	379,461
6 SANWA BANK	375,557
7 CREDIT AGRICOLE†	302,983
8 BANQUE NATIONALE DE PARIS†	289,747
9 CITICORP	216,914
10 CHEMICAL BANKING	135,459**

*As of Mar. 31 except as noted

**Pro forma

†12/90

cuddy. In fact, he and Shipley are already planning a \$1.25 billion stock sale and a possible takeover.

For rivals, the two chairmen long have been on good terms. Ever since their first meeting in a Kansas City steakhouse 20 years ago, McGillicuddy and Shipley have been running into each other. But they never talked about merging until 1989. McGillicuddy was preoccupied with selling 5% of his bank and 60% of CIT Group, Manny Hanny's finance arm,

themselves chatting over coffee. But now, Texas was turning a profit, and Manny Hanny's Japanese deals were closed. "So," says Shipley, "we decided to talk again." From such modest beginnings sprang the nation's largest-ever banking merger to date. Chances are the record won't stand for long.

By William Glasgall, with Suzanne Woolley in New York, David Greising in Chicago, Catherine Yang in Washington, and bureau reports

BUYING MERGER TARGETS: IT'S 'A DANGEROUS GAME'

Nothing makes the adrenaline pump like watching a stock shoot up 25% in one day. So, en Manufacturers Hanover Corp. pped 26% and Chemical Banking p. 16% after their July 15 merger announcement, investors felt the temp- on to find other banks about to do same—and buy in beforehand.

Bank stocks rose 5% in a day on h excitement (chart). Yet profes- als warn investors not to wrack ir brains wondering which bank will next. "To make merger potential r No.1 criterion is a dangerous ne," says George M. Salem, a Pru- tial Securities Inc. analyst. Despite essing games played by Wall eeters, analysts say there's no way spotting the marrying kind with ch certainty. And if you're wrong, a could be stuck with a Bank of New gland Corp. in your portfolio.

HEALTHY GLOW. Instead, think funda- ments. Money managers say the art picks now are banks with strong osit bases, high ratios of equity to ets, and profitable lending lines. ch banks should do well in any cli- te. And in an era of consolidation, y're in a good spot to snap up small-

er banks—or be snapped up them- selves. Examples on the list of Karen L. Finkel, portfolio manager of PaineWebber Inc.'s Regional Financial Growth Fund, include Keycorp in Albany, N. Y., which has low costs and a winning strategy of focusing on markets where it can dominate, and Chicago's Northern Trust Corp., which boasts a fee-based trust operation with little credit risk.

A favorite is Banc One Corp. in Colum- bus, Ohio, which has succeeded by focusing on retail lending and credit cards and by ac- quiring dozens of smaller banks. Shelby Davis, who manages the \$400 million New York Venture Fund Inc., is a Banc One bull. "I prefer companies doing the ac- quiring," he says. "You can only be acquired once. Companies doing the ac- quiring can do it again and again."

Investors may also thrive by keeping money on potential intramarket merg-

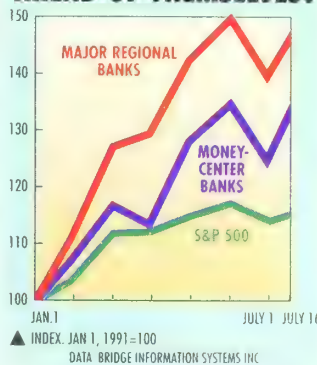
ers—those, as with Manufacturers and Chemical, that stand to slash overhead. One such possibility is the merger being mulled between Cleveland's National City Corp. and Ameritrust Corp.

For adventurers, patience is key. Davis says he's sticking to high- and medium- grade banks for now, including Banc One and Wachovia Corp. in Winston-Salem, N. C., in the first category and First Bank Sys- tem Inc. in Minneapolis in the second.

But if the recovery takes hold, Davis will get ready to reach for more speculative plays. "As the future gets clearer in terms of nonperforming loans peaking, you might trade down from the highest quality to medium grade and eventual- ly to the most troubled, some of which might turn around," he says. But re- member: The weaker a bank's balance sheet, the higher investors' risk.

By Andrea Rothman in New York

DID BANK STOCKS GET AHEAD OF THEMSELVES?



ON THE THRESHOLD OF A NEW ORDER

But what did Gorbachev take home from London? Not much

It seemed like old times. To the applause of the world, a smiling President George Bush and ebullient Soviet Leader Mikhail Gorbachev emerged from a chat at Winfield House, the U.S. ambassador's London residence, pledging to conclude a major arms-control pact and agreeing to yet another superpower powwow in Moscow before July is out. Ronald Reagan would have loved the scene, another chapter in the Big Thaw in East-West tensions. But Gorbachev's visit to the 17th annual Economic Summit of Industrial Nations isn't just another chapter. It's a whole new book.

The Big Thaw is officially over. Now comes the New Economic Order, and it promises to be even more slippery and perilous than what preceded it. The Group of Seven gathering ended on a high note—welcoming the Soviet leader, stressing unity on a host of global problems but papering over deep disagreements (table).

Gorbachev stayed behind in London to press his appeals for greater Western involvement in Soviet economic reform. The G-7 stage managers left town smiling, but wondering if the West will ever commit substantial amounts of its wealth to help the Soviets carry out the massive reform they envision. "It's still not clear that they have, at the political leadership level, the kind of understanding of the workings of a modern economy that is really necessary," says National Security Adviser Brent Scowcroft. Unofficial observers put it more bluntly. Said Harvard University political scientist Graham Allison, who co-authored a widely cited study on Soviet aid: "These guys are trying to fix a car, and they have been riding on a horse."

The summit was historic on several counts.

The two superpowers agreed to settle technical differences and sign a sweeping Strategic Arms Reduction Talks (START) treaty in Geneva later this year. The most significant arms-control pact in 20 years, it would be the first to cut, not just limit, the number of long-range missiles. It would also make it easier for the Soviet Union and the U.S. to reduce military spending, boosting U.S. efforts to cut its deficit and aiding Soviet plans to convert weapons plants to civilian use (page 42).

And with Gorbachev's ground-breaking visit, the economic affairs of eastern Europe and the Soviet Union will become a fixture at future G-7 meetings. The Seven agreed to grant the Soviets a sort of permanent-observer status in which the annual chairman of the group will maintain regular contact with Gorbachev or his successor.

FLYING SOLO. The assembled world leaders didn't strike a Grand Economic Bargain, though. With a cautious Bush leading the hard-liners, the G-7 withheld direct aid until the Soviet Union is ready to take radical economic steps. "We believe President Gorbachev has made an irrevocable commitment" to open markets, said Bush at a post-summit press conference. But he's waiting for the fol-



BEHIND THE SMILES THERE ARE DEEP DIVISIONS

low-through. Even some senior Soviet officials believe that Western financial aid is premature. Says Leonid Abalkin, a senior Soviet economist: "If we can achieve political stability and carry through radical reform on our own, one is capable of helping us."

Gorbachev probably advanced his



Their easy rapport helped Bush and Gorbachev come close to nailing down the START agreement



SCORECARD FROM THE LONDON SUMMIT

SOVIET UNION

AIDING MOSCOW The G-7 agreed to give technical economic assistance and offered the Soviets special status in the International Monetary Fund, which could lead to making the ruble convertible. But there is no consensus on paying to aid Soviet reform

ARMS CONTROL U.S. and Soviet officials agreed to reduce strategic weapons, setting the stage for a Bush-Gorbachev summit in late July

MIDDLE EAST

WARNING IRAQ President Bush emerged with support for another possible military strike aimed at Saddam Hussein's nuclear facilities

NEGOTIATING PEACE The G-7 endorsed Bush Administration efforts to broker a Middle East peace

UNFINISHED ECONOMIC BUSINESS

CUTTING FARM SUPPORTS The leaders couldn't break the deadlock over agricultural subsidies, raising the specter of hostile regional trading blocs

PROPPING UP EASTERN EUROPE The U.S. had hoped to promote reforms in former Soviet satellites. But Gorbachev's visit overshadowed that effort

use by avoiding any outright request for money. After Western leaders reject detailed aid requests from top Kremlin bureaucrats in the weeks leading up to the London summit, Gorbachev used soft sell. Bush and the other summiters expressed their appreciation of Gorbachev's restraint by not ruling out substantial future aid.

The West also pledged to send advisers to help overhaul the Soviet energy, transportation, and agriculture sectors. These are key to reviving the imploding Soviet domestic economy and creating a freely convertible currency, which could be the most effective incentive for Moscow to get its economic house in order and keep it that way.

The touchstones for the new era of East-West coordination will include regular consultations between high-ranking Soviet officials and G-7 economic advisers on such issues as the ruble and rationalizing prices. But the real task of helping a Soviet economic turnaround will be tied to the International Monetary Fund. Giving the Soviet Union a special status in the international lending agency, the IMF will become the key overseer of Soviet progress.

Gorbachev will now use the promise of Western aid to shore up his support at home. "This is a very important matter for the internal situation in the Soviet Union," says Yevgeny Primakov, Gorbachev's point man in London. "If we find support not just in words but in deeds from the West, it will absolutely strengthen the position of reformers."

Greater political stability would provide one of the preconditions the Soviets need to hit their target of making the ruble internally convertible on Jan. 1, 1992. And they're betting that the IMF and the West will eventually kick in \$12 billion to create a pool of funds to prop up their virtually worthless currency.

While U.S. officials remain wary of any sudden lurches toward direct cash aid, Bush is likely to give Gorbachev an additional boost when he visits Moscow for a July 30-31 summit. A senior Administration official who was in on Bush's discussion with Gorbachev says there is now a "chemical relationship" between Bush and Gorbachev that makes it easy for the two to talk frankly. That rapport helped them come close to nailing down the long-promised START agreement, which will cut by about 30% the number

of nuclear weapons in each side's arsenal, including a 50% reduction in the number of Soviet SS-18s. Those are the most threatening Soviet weapons because of their accuracy and power.

With START out of the way, Bush can turn his attention to cutting economic deals with Gorbachev and the Europeans. When Congress returns from its August recess, the President will press for Senate ratification of a treaty that would give the Soviet Union most-favored-nation trade status, freeing the Soviets from punitive import tariffs.

CLOSER LOOK. Jawboning Congress may be an easier task than persuading the Europeans to eliminate agricultural subsidies. While the G-7 leaders pledged to settle their differences on the issue, they made the same promise last year in Houston—before the General Agreement on Tariffs & Trade talks foundered over the question of farm aid.

Bush may find those problems mere small fry once he gets a firsthand look at Gorbachev's plight in Moscow. Achieving serious reform without inciting social upheaval could faze even so skilled an operator as Gorbachev. He faces "a truly enormous task," says

Under Secretary David Mulford. "The transition will be difficult, comprehensive, and time-consuming."

That's why the Europeans, with the Soviet Union on their doorstep, are far more eager to invest in reform than are the Americans or Japanese. And while the Kremlin's military threat has faded, the fear that the Soviet Union will devolve into a Yugoslavia with nuclear weapons gives Western leaders a compelling reason to help Gorbachev weather the transition.

Any number of domestic crises could weaken Gorbachev's stubborn hold on power. He returns home to a comatose economy, with output falling at an annual rate of 24% and inflation running at a

100% clip. Some Western bankers worry that when about \$12 billion of the Soviets' \$65 billion in external debt comes due this year, they may not be able to meet the payments, raising the specter of a demeaning rescheduling program. Public and private Western aid—which has amounted to about \$50 billion over two years—has virtually dried up.

The most immediate funding is likely to come from the new European Bank for Reconstruction & Development. Political uncertainty, along with conflicting national and regional laws on ownership and regulation, is turning off other investors. "Western companies are hanging fire," says Ronald Freeman, the EBRD's first vice-president, who in early

July accompanied 16 U.S. oil executive to the Soviet Union. "Gorbachev needs to tell his comrades that the message from the G-7 is that it's time to clarify legal issues and proceed to the market."

For Gorbachev, there's no turning back. When he returns home, he faces fierce hard-line opposition to his new engagement with the West. But at the least, Gorbachev has been invited to sit at the G-7 table. It took 20 years for the U.S. and the Soviet Union to work out a reduction in nuclear arms. Neither side can afford to wait that long for economic assimilation.

By Douglas A. Harbrecht, Richard A. Melcher, and Rose Brady in London, with Mike McNamee in Washington

HOW GORBY PLAYED ON THE LONDON STAGE

Even by his own dour standards, Mikhail Gorbachev's historic debut at the summit of the world's seven leading industrial nations was stark and sober. His 200-person entourage was small by summit standards. And when it checked into the Royal Gardens Hotel in London's Kensington district, the Soviets instructed hotel manager Roberto Varsalona to remove all the liquor bottles from the minibars in their rooms. "They've been cost-conscious," says Varsalona. "They don't want to be seen to be throwing money away."

No wonder. Gorbachev was attempting a painful balancing act: He wanted to maintain his dignity as the leader of a superpower while begging for advice and aid. And he was playing an especially weak hand. On the London financial markets, the Soviets' once-pristine credit rating had slipped to that of a backward Third World nation, and their economy had fallen into a trough worse than the Great Depression. Meanwhile, political factionalism still threatens to atomize Gorbachev's homeland, transforming it from a highly centralized union into an unruly collection of quarreling states.

BULGING BRIEFCASES. So Gorbachev's staff of economists, diplomats, and KGB officials had to present a buttoned-down image. And that they did. For several days before the boss arrived, they fanned out throughout London for intensive talks with leading bankers, finance ministers, and top aides to

the G-7 leaders. Their briefcases bulged with copies of new Soviet privatization and foreign-investment laws, used to bolster arguments that the moves to a market economy are serious and that the Soviets are worthy of big foreign investments. Gorbachev held intense 45-minute meetings with such leaders as Toshiki Kaifu of Japan and François Mitterrand of France.

Gorbachev's "sherpas" sometimes had trouble keeping their cool. Usually, top Gorbachev aide Yevgeny Primakov

Bush, he bridled when asked if he would be satisfied with political support and technical advice, or did he want a bundle of cash? Angered, Gorbachev grunted. When reporters broke into laughter, he barked: "That's my answer." Then he cut short the press conference.

WRONG TURN. Still, the G-7 meeting did stir some soul-searching among the Soviets about why East and West had been at loggerheads for nearly half a century. As part of summit preparations, Victor Geraschenko, chairman of Gosbank, the Soviet central bank, had his aides dig out the reason the Soviet Union didn't join the International Monetary Fund and World Bank back in 1946. The aides found in Soviet archives a letter written by Geraschenko's father, then a high government official, to Stalin. Geraschenko senior had urged Stalin to sign on with the financial institutions or face years of Soviet economic estrangement.

Stalin, eager to grab Eastern Europe, dug in his heels, saying the World Bank and IMF could be vehicles for the West to dominate the Soviets economically. When he got the letter, the junior Geraschenko instructed his staff: "Let's not make the same mistake again. Let's not distance ourselves from the West." Despite their prideful stiffness, Gorbachev and his entourage made a genuine effort to bridge that distance in London.

By Rose Brady and Richard A. Melcher in London



GORBACHEV LOBBYING MITTERRAND: TRYING TO BEG WITH DIGNITY

jets from one Middle Eastern capital to another, brokering Soviet diplomatic policy. But when British bankers seemed to patronize him during meetings in London, his feathers got ruffled. "I got the impression they are getting ready to buy up huge assets cheaply. It's like when Columbus went to America. But we are not the Indians. We will not be bought cheaply."

Gorbachev himself showed glimpses of quintessential Russian touchiness. At a press conference with George

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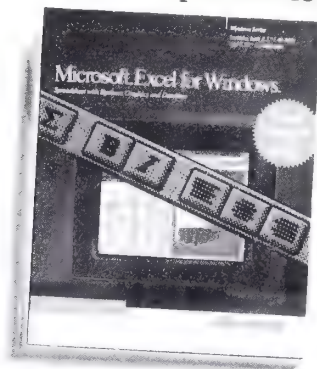
January 1991

Volume 8.1

Advanced Spreadsheet Programs

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2nd	2.0	Quattro® Pro	8.4
3rd	3.1	Lotus® 1-2-3™	7.2

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ROBERT MAXWELL TAKES A LONG STEP BACK

Debt may force him to spin off much of his U.S. media empire

Cash is king," advised Robert Maxwell after the October, 1987, stock market crash. Too bad he didn't heed his own words. Barely a year later, the British publishing mogul embarked on an astounding buying spree, paying \$3.35 billion for book publisher Macmillan Inc. and Official Airline Guides Inc. All of the money for these acquisitions was borrowed.

Now, the load of debt is crushing Maxwell. The recession and a steep drop in the value of publishing properties have left his publicly held company, Maxwell Communication Corp., in a bind: MCC is struggling to generate enough cash from core operations to service its \$2.1 billion in debt (table). Maxwell can't sell enough assets at top prices to lower the debt. So analysts have been waiting anxiously to read Maxwell's annual report and see how deep its problems run.

FAILED PLAN? The annual arrived on July 16, and with it, a bombshell: A vague plan to spin off Maxwell's North American assets, including Macmillan and OAG. Maxwell won't provide details. But analysts in London and New York speculate that Maxwell might spin off Macmillan and OAG into a separate company, then sell a chunk of that in a U.S. public stock offering. Maxwell claims a sale would "realize shareholder values." But investors are anything but cheered: Within a day of the announcement, MCC's share price plummeted 6%.

The plan may signal that Maxwell's grand scheme for a global media empire is fading. Macmillan, OAG, and the North American properties contribute 90% of MCC's operating profits. What's more, the announcement made clear the new company would be managed by Americans, not Maxwell or his son and heir, 32-year-old Kevin Maxwell. MCC, which is 68% owned by Maxwell, could retain a majority stake. But confidantes believe the family will accept a smaller role in return for easing the debt. "They are fed up with constantly worrying about the debt," says one adviser. "They have not enjoyed the last two years."

Maxwell's retrenchment comes after

an embarrassing flip-flop on his succession. In April, the 68-year-old publisher said he would step down as chairman on July 1 in favor of Sir Peter Walker, a former British cabinet minister. Bankers close to the company say Walker later looked at the books and suggested that the company's finances be shored up. Walker and Maxwell say they agreed on



MAXWELL: STRUGGLING TO MEET THE INTEREST ON \$2.1 BILLION

the spin-off plan, but Walker now says he no longer sees a role for himself in a shrunken MCC. So Maxwell will stay on as chairman, while his son will become chief executive.

Like Rupert Murdoch and other acquisitive media barons, Maxwell simply paid too much for his purchases. With a \$1.3 billion debt payment due in 1994, Maxwell must raise cash. He already has sold off Pergamon Press and other

holdings that formed the bulk of MCC prior to its Macmillan purchase.

Nor can Maxwell look to his private companies for help. Those companies whose holdings include New York's *Daily News*, are lumbering under their own \$1.1 billion debt. And several media analysts say the *Daily News* continues to hemorrhage money three months after Maxwell bought it from Tribune Co. and settled its labor strike.

Analysts note that MCC's results in the year ended Mar. 31, 1991, hardly inspire confidence. The company reported pretax profits of \$240 million. But much of that came from a onetime \$133 million foreign-exchange windfall. Subtract other nonrecurring items, such as sale investments, and MCC's profits were less than \$10 million. Analysts worry that cash flow will be negative this year. "They're in trouble," says one London analyst, "no doubt about it."

Given all that, American investors may not rush to become Maxwell's partner. Maxwell is still smarting from the 26% drop in the shares of Mirror Group Newspapers Ltd., another Maxwell company whose stock was floated last May in Britain and the U.S.

Another potential roadblock to the sale is the harm it could do to Maxwell's balance sheet. MCC's annual report claims a net worth of \$1.8 billion. But

that's after assigning \$3.4 billion worth of intangible value to Macmillan, OAG and other acquisitions. With the decline in the value of publishing assets, those intangibles are almost certainly overstated. Selling off companies for less than their book value would force Maxwell to take a write-down on the difference.

HURDLES LOOM. For example, Maxwell values his half of a textbook joint venture with McGraw-Hill Inc., publisher of *BUSINESS WEEK*, at \$670 million. But publishing industry executive familiar with the venture believes it could only be taken public for \$1 billion, meaning Maxwell's half is worth only \$500 million. So he faces a potential \$170 million write-off if he were to sell or float this venture. The cumulative effect of such write-offs could leave Maxwell with an even weaker balance sheet.

With such hurdles looming, some who know Maxwell wonder if his latest plan will ever emerge from the drawing board. Indeed, the erratic publisher has a history of announcing deals and not following through. This time, though, he may have few other choices.

By Mark Maremont in London, with Mark Landler in New York

MAXWELL'S CASH-FLOW WOES

Fiscal year ended March, 1991

Millions of dollars

Gross cash flow	\$539
LESS nonrecurring cash inflows	-216
EQUALS cash flow from ongoing media operations	323
LESS net interest expense, dividends, imputed taxes on core operations, and other	-446
Cash drain from ongoing media operations	-123

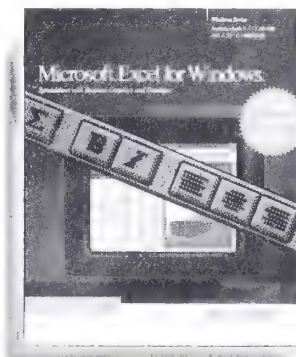
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Commentary/by Paul Magnusson

THE ANTITRUST BALL AND CHAIN HOBBLING HIGH TECH

Back in 1989, when U.S. Memories was struggling to get off the ground, President Sanford L. Kane wasn't too worried about the chipmaking consortium running afoul of antitrust laws. After all, most U.S. semiconductor makers were unconditionally surrendering the memory-chip market to the Japanese. Kane figured that organizing a group of American outfits in a last-stand effort to manufacture the next generation of memory chips could only be welcome news.

Kane sees a sad irony in that. If the domestic industry hadn't been on its last legs, "we would have had a hell of a time convincing the partners that joint production wouldn't lead to antitrust problems." So, Kane asks, why not help encourage U.S. industries to stay healthy?

Well, why not? Although U.S. Memories didn't fly, the idea of cutting-edge companies banding together to match the deep-pocketed clout of their foreign rivals makes good sense. So what's stopping the nimblest U.S. companies from linking arms? Mainly, the risk that a customer or a producer left out of the action will file a costly antitrust suit. Under the Sherman Antitrust Act, an injured party can collect triple any actual damages—a potential disaster to a small, innovative company.

RISK RELIEF. The Administration has proposed, and Congress is poised to pass, a remedy: the National Cooperative Production Act. The legislation recognizes the reality of modern high-tech manufacturing. For example, with the cost of gearing up to make advanced memory chips rising toward \$1 billion, the lone-wolf era may be over (chart). Only with collective action can U.S. chipmakers stay competitive with huge, vertically integrated Japanese electronics companies that have used the profits from TV sets, laptop com-

puters, and cellular telephones to fund the next generation of chips.

It's not just the chipmakers who are feeling chummy, either. Spreading the financial risk could also be an attractive option for companies in such capital-intensive industries as robotics, machine tools, and high-definition television. For these businesses, the bill has two key provisions. It would relieve government-sanctioned joint ventures from treble-damage phobia. And it would write into law various court decisions that have cast a warm-

tion for Joint Manufacturing, an industry group.

A more finely crafted restriction might satisfy all sides. The ownership issue could be finessed by allowing participation of foreign companies in ventures here if their government permit U.S. companies to participate in similar joint ventures abroad. The Administration has already used such a fair-is-fair standard in deciding who's eligible for government funds for its new Advanced Technology Program.

Some critics, such as Representative

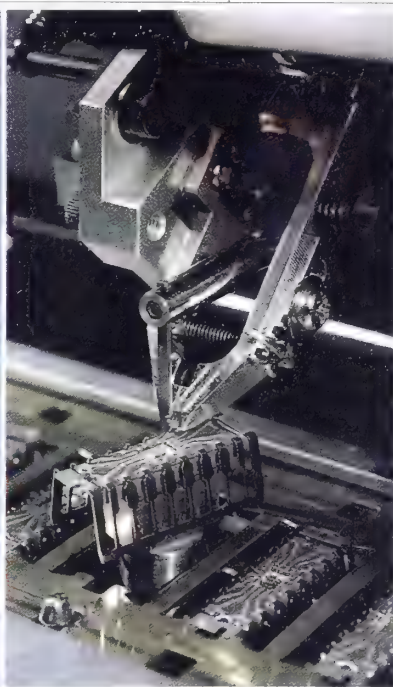
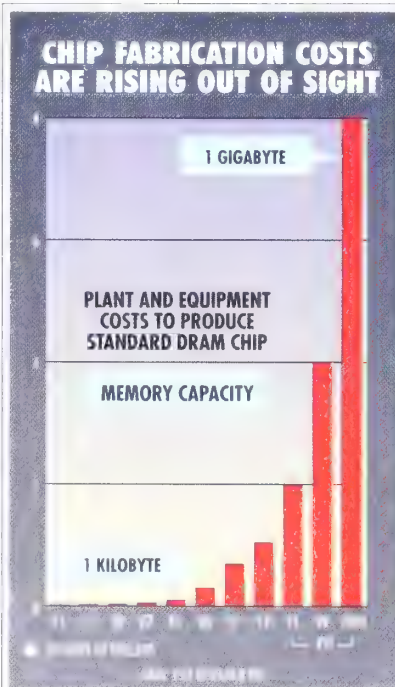
Mike Synar (D-Okla.) argue that the legislation is unnecessary because current law leaves plenty of room for joint production. They cite the General Motors-Toyota joint venture in Fremont, Calif., and the plan by IBM and Apple Computer for joint development of next-generation software and hardware. Indeed, the Commerce Dept. says some 50 joint-manufacturing efforts are announced each year.

But these are older and larger companies with experience at cooperative ventures. It's the smaller companies with the crucial innovations that balk, recognizing that tre-

ble damages are a magnet for costly lawsuits.

Easing the legal threat would also help U.S. high-tech companies become more competitive in world markets. In Japan, government and private antitrust suits are rare, and plaintiffs are limited to actual damages. In Europe, joint-production ventures can be granted absolute immunity from all antitrust suits.

This modest proposal before Congress hardly threatens the nation with a new generation of robber barons. Current legal constraints against collusive activities would still apply. But for a few high-tech industries, a little freedom from fear of triple damages may be all that's needed.



er eye on joint-production accords.

Trouble is, a last-minute dispute over whether the provisions should apply to foreign companies is threatening to draw a White House veto. The version approved by the House Judiciary Committee would exclude co-production ventures with more than 30% foreign ownership. At a time when the U.S. is demanding that its trading partners drop barriers to foreign investment, such a provision would be a major embarrassment. The bill's supporters—Intel, IBM, and Compaq among them—aren't happy about the provision, either. "Some foreign firms may bring to the table the very technology—and the capital—that we are looking for," says Ted Heydinger, director of the Coali-

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Jim Seymour. *PC Week*, January 28, 1991.

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AMERICAN IN LONDON: FACING HIGHER COSTS, DELAYS, AND MARKETING HURDLES

EUROPE WON'T BE A JOYRIDE FOR THE YANKS

Why United, American, and Delta have their work cut out for them

As the breakup of once-proud carriers such as Pan Am continues, hope abounds among U.S. successors that they will once again dominate the world's skies. American, United, and Delta have earned the rights to succession. But as they buy assets and gear up for transatlantic expansion, what will it take for them to succeed where the pioneers have failed?

The work is just beginning for America's new flag carriers. Certainly the big three U.S. airlines have far greater wealth and reach than Pan American World Airways Inc. or Trans World Airlines Inc. ever did. But they must grapple with a dizzying array of marketing challenges, steeply higher operating costs, and stiff competition from the likes of British Airways PLC. How they master the nuts-and-bolts issues of expansion will determine how seriously they contend for transatlantic supremacy. Concedes UAL Corp. Vice-Chairman John C. Pope: "It'll be a very tough market."

That's not stopping the rush to Europe. In 1990, United Air Lines Inc. served only Frankfurt and Paris. Today,

thanks to routes it bought late last year from Pan Am, it flies daily to London from five U.S. cities and offers connections to four other European cities. American Airlines Inc., with its purchase of TWA's London routes, and Delta, which agreed on July 11 to pay \$260 million for Pan Am's remaining European routes, are staging similar expansions (table). They're lured by stronger passenger growth than in the U.S. and the chance to build global networks.

Expansion, however, means more than just buying routes. Many Europeans have never heard of Delta, American, or United, and many Americans don't consider them when planning a trip to Europe. That's forcing the carriers to crank up marketing efforts reminiscent of political campaigns. American, which is

spending more than \$10 million on a name-recognition drive in Britain, gave away 500 free tickets to Chicago movie and shakers at a Windy City banquet on July 16. United, which is lavishing Dom Perignon champagne on first-class transatlantic passengers, initiated its London service in April by offering two-for-one deals to first- and business-class fliers and double mileage to its frequent fliers.

That's fine for an initial splash, but long-term gains will take patience. State-owned carriers such as Lufthansa have deep ties to travel agents and tour operators, who are often wary of the Americans. To butter them up, Delta has flown German travel agents to Orlando's Walt Disney World and served them a Southern feast of Charleston crab cakes in Berlin. But, says Lufthansa spokesman Wolfgang Weber: "We don't have to be afraid of competition."

TIGHTER SECURITY. Marketing challenges pale in comparison to a frightfully long list of added costs in Europe. Landing rights during peak hours at London's Heathrow Airport run up to \$10,000 for a Boeing 747, compared with \$1,190 at Chicago's O'Hare International Airport. To protect against the threat of terrorism, United alone plans to spend \$11 million this year on everything from guards to electronic scanners at Heathrow. Wage rates for baggage handlers and maintenance workers are 20% higher in Europe than in the U.S. Jet fuel is up to 5¢ a gallon more expensive. And unlike the U.S., where air-traffic-control fees are partly paid out of a ticket tax, airlines in Europe pay a per-flight fee for control services.

The European air-traffic-control system should also challenge the scheduling skills of U.S. carriers. Largely because of air-traffic snarls, over 25% of all flights in Europe departed late during peak periods last summer, compared with about 13% in the U.S. Delays mean underused planes and ticked-off passengers, costs not easily seen on an income statement.

Despite these problems, the Yanks sound ready. Says American Chairman Robert L. Crandall: "Airlines in Europe

don't know anything about real competition." That's a bit strong. And considering the hassles and extra costs, the American carriers may have to learn a few new tricks to compete in the Old World.

By Kevin Kelly in Chicago, with Mark Maremont in London and Chuck Hawkins in Atlanta



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WILL CHINA REMAIN A MOST-FAVORED DICTATORSHIP?

Congress wants to punish Beijing. Bush and business are fighting back

Call it the rubber-sole lobby. Its motto: "Don't tread on my sneakers." At the behest of shoe importers, tens of thousands of Americans have flooded Capitol Hill with form letters begging Congress not to revoke China's most-favored-nation trading status. These amateur lobbyists may not know much about foreign policy. But they know that the local Wal-Mart sells low-priced shoes made in China, and they fear an approaching Senate vote might cut off the supply of inexpensive sneakers. The grassroots effort may be having an impact: "These days," says a top Senate Democratic aide, "nobody wants to be blamed for raising costs to the middle class."

The letter-writing campaign is part of a broad effort by corporations trying to defend \$40 billion worth of investments and \$15 billion in annual trade with China. It's an uphill fight. A majority on the Hill wants to punish China for the 1989 Tiananmen Square massacre. The House has overwhelmingly passed a bill that would impose a long list of conditions on President Bush's proposed extension of MFN status for China. The Senate is expected to approve a similar measure by the end of July. But it's not at all certain the margin will be enough to assure an override of the expected Bush veto.

China has few friends left in Washington. Both liberals and right-wingers are out to condemn Beijing for human-rights violations and for stepping up sales of missiles to volatile Third World nations. Trade hawks are upset at China's growing trade surplus with the U.S., which amounted to \$2.2 billion in the first quarter of 1991.

CONVERTS. Bush argues that continued Western economic links are vital to keeping China's reform movement alive. Business executives, trooping to the Hill after visits to plants in China, echo that message. Nike Inc. President Richard Donahue, just back from a China foray, says that exposing Chinese workers to capitalism "is the best way to ensure the downfall of a totalitarian government."

The pro-MFN lobby is picking up some converts by focusing on a dozen or so fence-straddling Southern and Midwestern senators. It has already won over two key Southerners, J. Bennett Johnston (D-La.) and Richard C. Shelby (D-Ala.), whose states sell petrochemicals and fertilizers to China. And wheat growers, who annually export 6 million metric tons of grain to China, gained the support of North Dakota Democrats

150 MD-90 aircraft to Beijing. Loss of MFN, its lobbyists say, could kill a deal worth \$7 billion—and cost jobs in the U.S. "You bet we've been active on this," says one lobbyist. Boeing Co. has also mobilized. At a Beijing lunch last month, Premier Li Peng bluntly warned an official of the Seattle company that he would end talks on a 13-plane order worth \$800 million if MFN is jeopardized.

CONCESSIONS? Pro-MFN forces have also enlisted a group of foreign policy luminaries, including three former ambassadors to Beijing and onetime Defense Secretary Frank C. Carlucci III. In a letter to all senators, they urge an unconditional extension of trade privileges. Former Secretary of State Alexander M. Haig Jr. organized the drive. The letter fails to mention that Haig is a consultant to United Technologies Corp., whose Pratt



McDONNELL DOUGLAS ON THE MAINLAND: A \$7 BILLION DEAL AT STAKE?

WHAT CHINA SHIPS TO THE U.S.



Quentin N. Burdick and Kent Conrad.

Importers and exporters are approaching the issue from opposite sides. Nike, which makes about 10% of its shoes in China, and giant retailers Toys 'R' Us and J.C. Penney argue that trade restrictions will hurt U.S. consumers by driving up the cost of Chinese goods. Exporters insist that sanctions would result in the closing of the Chinese market, forcing a cut in U.S. production and employment.

China is pitching in, too. It has hired the public-relations giant Hill & Knowlton Inc. for \$150,000 a month. U.S. companies, however, carry more weight on the Hill than China's hired guns. After four years of negotiations, McDonnell Douglas Corp. is close to a deal to sell

& Whitney unit would make the engines for the planes McDonnell Douglas hopes to sell to China. A Haig spokesman says there's no connection between the letter and Haig's work for UTC.

Business might succeed in tipping the scales to the White House. But to help ensure success, the pro-MFN forces are urging Bush to offer concessions. One possibility is intensifying a federal investigation of China's treatment of U.S. patents and copyrights. Another involves granting Taiwan observer status in the General Agreement on Tariffs & Trade. That might just be enough to give Bush the 34 senators he needs to sustain a veto. If the President can thwart an override, business lobbyists and their footsoldiers in the sneaker battalions can claim considerable credit.

By Paula Dwyer in Washington, with Dori Jones Yang in Seattle and bureau reports

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JUNK HIJINKS AT BURLINGTON?

► The Securities & Exchange Commission is investigating alleged insider trading in the junk bonds of Burlington Holdings. The inquiry, which SEC staffers confirmed on July 16, is part of an informal look at trading abuses in the high-yield debt market.

The agency is questioning alleged trading by two New England-based institutions on the afternoon of July 3. In the hours before Burlington announced a debt-restructuring plan, the institutions allegedly tried to load up on Burlington bonds. After the restructuring was announced, prices of the company's 13.875% senior subordinated notes surged from 68¢ on the dollar to 72¢. The agency wants to know what institutions were involved and whether they had nonpublic information about the restructuring.

HOW AZT COULD GO GENERIC

► As the sole holder of the patent on AZT, Burroughs Wellcome has made nearly \$1 billion since 1987 selling the only drug approved to treat AIDS. The National Institutes of Health, whose staff did most of the initial testing and development of the drug, says it should share the patent.

The agency backed up its argument on July 11 by licensing tiny Barr Laboratories to make generic AZT. The agreement will bolster Barr's case in its court battle with Burroughs over the smaller company's right to sell the generic drug. Burroughs had no comment.

PULLING THE PLUG ON TUCSON ELECTRIC

► Here's a variation on the midnight raid. At 12:14 a.m. on June 16, three major creditors of Tucson Electric Power

sued to put the utility into involuntary bankruptcy. Tucson Electric had been negotiating since late January with its creditors, including coal suppliers and bond holders, for a major restructuring plan. In the interim, TEP had stopped paying most of its bills.

The creditors who filed the petition included Ford Motor Credit and Philip Morris Capital, which had invested in sale-leasebacks of Tucson Electric power plants. The filing followed the power company's decision to stop making lease payments. Tucson Electric executives have 20 days to respond to the petition. The utility could, they acknowledge, file its own bankruptcy plan.

TRAVELERS AND McCALL MAKE UP

► An ugly fight over a failed LBO has ended with an unusual settlement. Back in September, 1987, Travelers Insurance lent \$35 million to Crowthers McCall Pattern. When the sewing-pattern business went into Chapter 11 the next year, Travelers sued former McCall Chairman Reginald Lewis (now head of TLC Beatrice International), accusing him of keeping two sets of books. The New York financier, who sold McCall to John Crowther Group in June, 1987, countersued Travelers for libel.

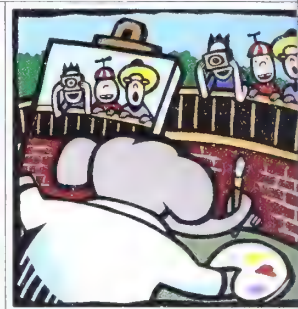
On July 16, both parties

PLEASE DON'T FEED THE ARTIST

Meet the Phoenix Zoo's artist-in-residence. Her medium is acrylic on canvas, and she works in natural light. Her colors range from the sunbaked pastels of the Southwest to bright primaries. Her paintings are notable for their energy and free use of white space. The artist's name is Ruby. She's an Asian elephant.

No, really. Ruby started painting in 1987, after a keeper noticed her penchant for making marks in the sand with her trunk. Now, she paints about once a week, using her trunk both to make brushstrokes and indicate her choice of brush and color to her keepers. An original Ruby can cost as much as \$1,200, with proceeds going into a fund for endangered species.

Other elephants at the zoo have tried painting, but with far less success. In fact, Ruby once painted over another elephant's rather perfunctory effort, then added a few touches of her own. Zoo staffers call that work "The Critic."



agreed to drop their suits. The settlement calls for each to make undisclosed donations to a charity of Lewis' choice. But separate suits against Lewis by U. S. Trust and McCall itself are still pending.

POLLUTION CREDITS WILL HIT THE PITS

► The Chicago Board of Trade on July 16 approved a plan to trade the allowances granted by the Environmental Protection Agency to emit sulfur dioxide. Under the 1990 Clean Air Act, companies with emissions below the legal limit would be able to sell EPA cred-

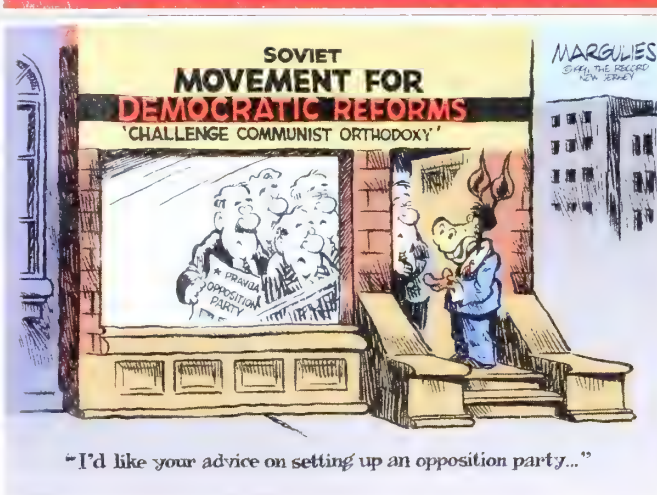
its to companies whose emissions exceed the clean air standards.

The board hopes to open a spot market in the allowances by 1992. Says Richard Sandor, a Kidder Peabody executive managing director who helped develop the concept: "We're taking something Americans are best at, financial engineering, and using it to address social problems."

AT&T: STATIC FROM ENVIRONMENTALISTS

► Consumers are asking AT&T to "put it in writing." The National Environmental Law Center on July 12 presented AT&T with 20,000 postcards asking the company to publicize its environmental record—good and bad.

The NELC says that since AT&T is trumpeting its efforts to phase out ozone-destroying chlorofluorocarbons, it should also let consumers know its status under other environmental laws. That would include telling the public of recent violations of the Clean Water Act in New Jersey. Several other environmental organizations privately say that they, too, intend to step up scrutiny of corporate environmental claims.



ROBERT GATES IS ON THE BENCH, NOT OUT OF THE GAME

It looks as if Robert M. Gates has been hung out to dry. On July 16, the Senate and a reluctant President Bush agreed to delay hearings on his confirmation as Director of Central Intelligence until mid-September. That means Gates will have to spend the next two months in silence while allegations swirl anew about his role in the suddenly revived Iran-contra scandal.

But don't write Gates off just yet. While many Democrats are deeply suspicious of the veteran intelligence official, Senate Intelligence Committee Chairman David L. Boren (D-Okla.) remains a backer. "There is nothing I have seen at this point that would be disqualifying," Boren says. Agrees committee member Alan Cranston (D-Calif.), no friend of the Administration: "I'm inclined to be supportive at this time."

Even with Boren's support, the White House faces an uphill fight. The big challenge is to convince senators that Gates, then deputy director of the CIA, didn't know until October, 1986—just before the scandal broke—that profits from the sale of arms to Iran were diverted to Nicaraguan *contras*. The trial strains credulity because Gates's boss, late CIA Director William J. Casey, organized the operation. And former Central American task force chief Alan D. Fiers said in early July that he was prepared to testify that he informed a Gates subordinate, then Operations Director Clair E. George, about the diversion.

LAND MINES. The key to the White House strategy is stressing the CIA's "compartmentalization." Bush aides will argue that Casey's obsessive secrecy made it possible for Gates to be ignorant of something known to those above and below him. Both former CIA Director William Colby and Casey's former aide, Bobby R. Inman, support this contention. Says Inman: "Gates was cut out at the beginning of the Central American project" and learned of a secret operation "only because it was so large." The White House will also insist that Gates was backpacking in Washington State during the crucial days of August, 1986, when Fiers said he told George of the diversion. This can only work, however, if no more land mines go off under Gates. Independent Counsel Lawrence E. Walsh, whose Iran-contra probe is winding down, could end his inquiry with

some bombshell indictments. Intelligence Committee staffers are also looking into charges that Gates hindered an investigation of the failed Bank of Credit & Commerce International, perhaps because the CIA used BCCI as a conduit.

By sticking with Gates through what is certain to be a hot and unpleasant summer, Bush is risking new revelations and, perhaps, an embarrassing defeat. But for now, both the President and his nominee are prepared to hunker down while Washington's long knives are unsheathed.

By Paula Dwyer and Amy Borrus

UP IN SMOKE: \$500 BILLION IN BUDGET CUTS

Remember the nearly \$500 billion in deficit reduction achieved after weeks of bone-crushing budget negotiations last year? New figures released by the Bush Administration on July 15 show that most of the savings have gone a-glimmering—and that the deficit next year will be a stunning \$348 billion.

Taxes were the hardest-fought battle of the budget war, and in the end, Congress passed \$158 billion in miscellaneous hikes. But, analysts say, most of that revenue increase is being offset by lower-than-expected receipts. The problem: Although the economic assumptions behind the budget seem to have been reasonably accurate, forecasters overestimated personal income and therefore Social Security and income-tax revenues. On the spending side, the costs of bailing out bank and thrift depositors were greatly underestimated, and so were Medicaid outlays.

Still, no one wants to revisit the painful subject of deficit reduction—at least not until after the 1992 election. By sweeping the dreary business under the rug for at least two years, says budget-watcher Stanley Collender of Price Waterhouse, "the agreement worked perfectly."

By Howard Gleckman

PITAL WRAPUP

CONGRESS

On the surface, the election of David E. Bonior (D-Mich.) to succeed the retiring William H. Gray III (D-Pa.) as House Majority Whip was an amiable enough affair. In fact, the fight between Bonior and Representative Henry H. Hoyer (D-Md.) exposed deep rifts among House Democrats. Bonior was the candidate of the House Establishment and was backed by most key committee chairmen. But younger members and Southerners, who tended to favor Hoyer, feel increasingly alienated. Gray's resignation leaves blacks without representation in the leadership, and women seem as far as ever

from real power in the House. Speaker Thomas S. Foley (D-Wash.) may seek to ease tensions by naming a black and a woman as Bonior's top deputies.

SECURITIES

Baltimore investment banker J. Carter Beese Jr. is emerging as an early contender for a vacant Securities & Exchange Commission seat. Beese is a principal with Alex. Brown & Sons, serves on the SEC's Emerging Markets Advisory Committee, is a director of the Overseas Private Investment Corp., and has been a major fund-raiser for Republican candidates. Sources say his candidacy is being pushed by the Treasury Dept.

JOB SAFETY

Most executives think of the Occupational Safety & Health Administration mainly in connection with factories and construction sites. But OSHA rules could soon have a major impact on offices. Early next year, OSHA will serve notice that it is developing regulations to cover a wide range of workplace ergonomics issues. The goal: to reduce illnesses and injuries associated with office jobs, including work at video-display terminals. New rules may cover four broad areas: analysis of work-site risk, hazard elimination, medical monitoring of employees, and worker training to reduce injuries.

CAN GORBACHEV POUND MISSILES INTO PLOWSHARES?

His economic reforms—and Western aid—may hinge on retooling the vast Soviet defense industry



ASSEMBLING A MIG 29. OFTEN, THE ONLY FACTORY IN TOWN IS A DEFENSE PLANT

Rows of ominous gray surface-to-air missiles stand ready for shipping in a pristine, eight-story industrial shop of the Arsenal defense factory in Leningrad. But General Manager Vyacheslav Petrov would much rather show a rare foreign visitor his more benign goods: flour-milling machines put together by the plant's state-of-the-art machine tools. "No one else in the Soviet Union can make these. The market is huge," says Petrov, a lean, 53-year-old rocket engineer.

With the cold war over and the Soviet economy imploding, Petrov is a symbol of the agonizing bread-or-missiles dilemma confronting the world's most extensive military-industrial complex. Like thousands of Soviet defense factories, Arsenal is poised to undergo a wrenching transformation. Orders for its ship cannons, spy satellites, and missiles have been cut in half over three years. Thousands of jobs are threatened. To survive, Arsenal managers want to shift a large chunk of their operation

into civilian production. "The people, the equipment, the plant—everything has to change," declares Petrov. That means breaking free of the decades-old Soviet model in which Moscow dictates everything from raw materials to new products. **'SURROUNDED.'** All easier said than done. When Petrov tried to link up with a French company interested in the rocket-engine components Arsenal makes, the Defense Ministry in Moscow scotched the deal. When Petrov tried to make more machine tools for civilian appliance production, the Defense Ministry insisted that 75% of his workers keep laboring on weapons. "I'm still surrounded by the KGB and the military," gripes Petrov.

This is the reality that dogged President Mikhail Gorbachev as he appealed to the industrial world's leaders for up to \$40 billion in Western funding to help with defense conversion (page 28). For decades, the Kremlin has poured its best talent, its raw materials, and much of its research funds

into the military. So much of the Soviet economy goes into defense that estimates of the share range as high as 52% of gross national product. Until military factories start producing high-quality civilian goods, the Soviet economy will remain profoundly crippled—and the West's goal of permanently defusing the Soviet military threat unrealized. "Our idea of defense conversion is to take the Soviet plant, shut the door, and build another one next door to produce civilian goods," says a senior Bush Administration Soviet specialist.

If Gorbachev wants to get substantial Western funds for defense conversion, he must ensure that the money won't be secretly used to beef up the Soviet military capability. Instead of dismantling unnecessary weapons assembly lines, some Soviet generals and factory directors want to retain as much defense capacity as possible.

Their clout shouldn't be underestimated. Defense plant capacity hasn't changed even though the government says it has

orders for military equipment by about 10% in the last three years. And raising the defense sector's civilian-goods production doesn't necessarily mean major reductions in weapons capability. For at least 30 years, "dual use" defense factories have produced consumer goods from cars to snowmobiles. The General Machine Building Ministry, which oversees building strategic nuclear missiles, also makes 60% of all snowmobiles. Most Soviet TV sets and VCRs come from defense factories. "The average Soviet doesn't know that the popular Vytash washing machine is made by a defense factory. They only know it's a sturdy product," says Masha Myasishcheva, a retired defense worker in Moscow.

What's more, given pervasive secrecy, no one really knows how extensive the conversion of military plants really is. Soviet officials say 600 enterprises are involved. But that "probably represents no more than 10% of the total defense industry," says Malcolm Mackintosh, a senior research fellow at London's International Institute of Strategic Studies. Secrecy is so extreme that until last year, the Arsenal plant, with 12,000 workers, was identified only by an anonymous mailbox number.

TITANIUM SLEDS. Part of the difficulty of converting to full-fledged civilian-goods production is that long insulated defense-plant managers have little idea of what is practical to sell on the world market. They come up with fantastic proposals to build submarines with windows for tourists and T-72 combat tanks transformed into pavement-paving 45-ton fire engines. One factory attempted to make children's sleds. But the only metal the factory had on hand for sled runners was extremely expensive titanium, normally used for jet fighters.

So it is a distinct minority of Soviet defense products that can be switched to civilian use and are of high enough quality. These include space vehicles, metals, radar, and robot tractors capable of working in radioactive conditions. Here is where Western investments could make a major difference. A small but growing group of entrepreneurial defense-factory managers want what they call "real conversion." Such managers at Arsenal and other factories want contracts for military orders while also being free to make new civilian products and deal directly with foreign companies.

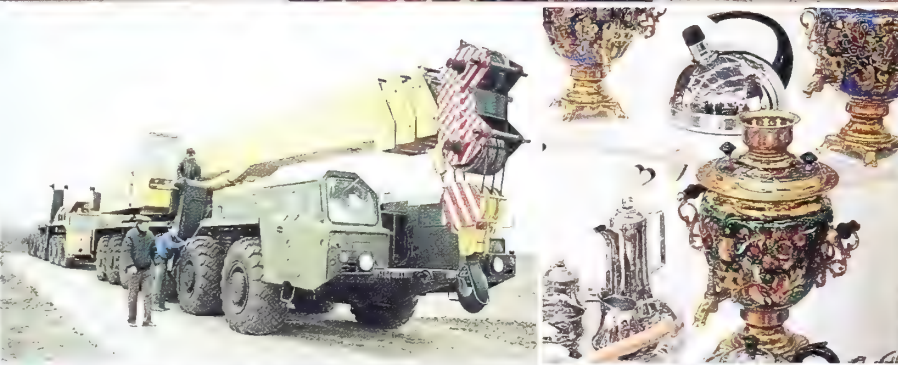
Likewise, Leningrad's Radium Institute, a key Soviet research facility for nuclear energy and power, is stepping up efforts to seek out new markets for its research. "We have important R&D developments, and we must find ways to commercialize them," says its director, Alexander Karelin. They include technology to make superconducting materials for high-energy magnets and for producing computer chips.

At least one defense plant has managed to divorce itself completely from the Defense Ministry. The Saratov Aviation fac-

tory, a former producer of military aircraft, has set up a joint-stock company to fund its production of Yak 40-passenger jets. Other defense factories are creating civilian spin-off companies, such as the Leningrad Optical & Mechanical Amalgamation, which produces military optics and lasers. Its new company will manufacture microscopes.

Boston-based Batterymarch Financial Management is including some of these projects as possible investment opportuni-

ties for its new Soviet-companies fund. Batterymarch trustee Dean LeBaron says he expects by year-end to raise the first \$250 million of a \$1 billion fund to turn Soviet defense technologies to civilian use.



■ SOVIET DEFENSE PLANTS PUMP OUT EVERYTHING FROM TV SETS TO SAMOVARS TO CRANES CONVERTED FROM MISSILE LAUNCHERS

ties for its new Soviet-companies fund. Batterymarch trustee Dean LeBaron says he expects by year-end to raise the first \$250 million of a \$1 billion fund to turn Soviet defense technologies to civilian use.

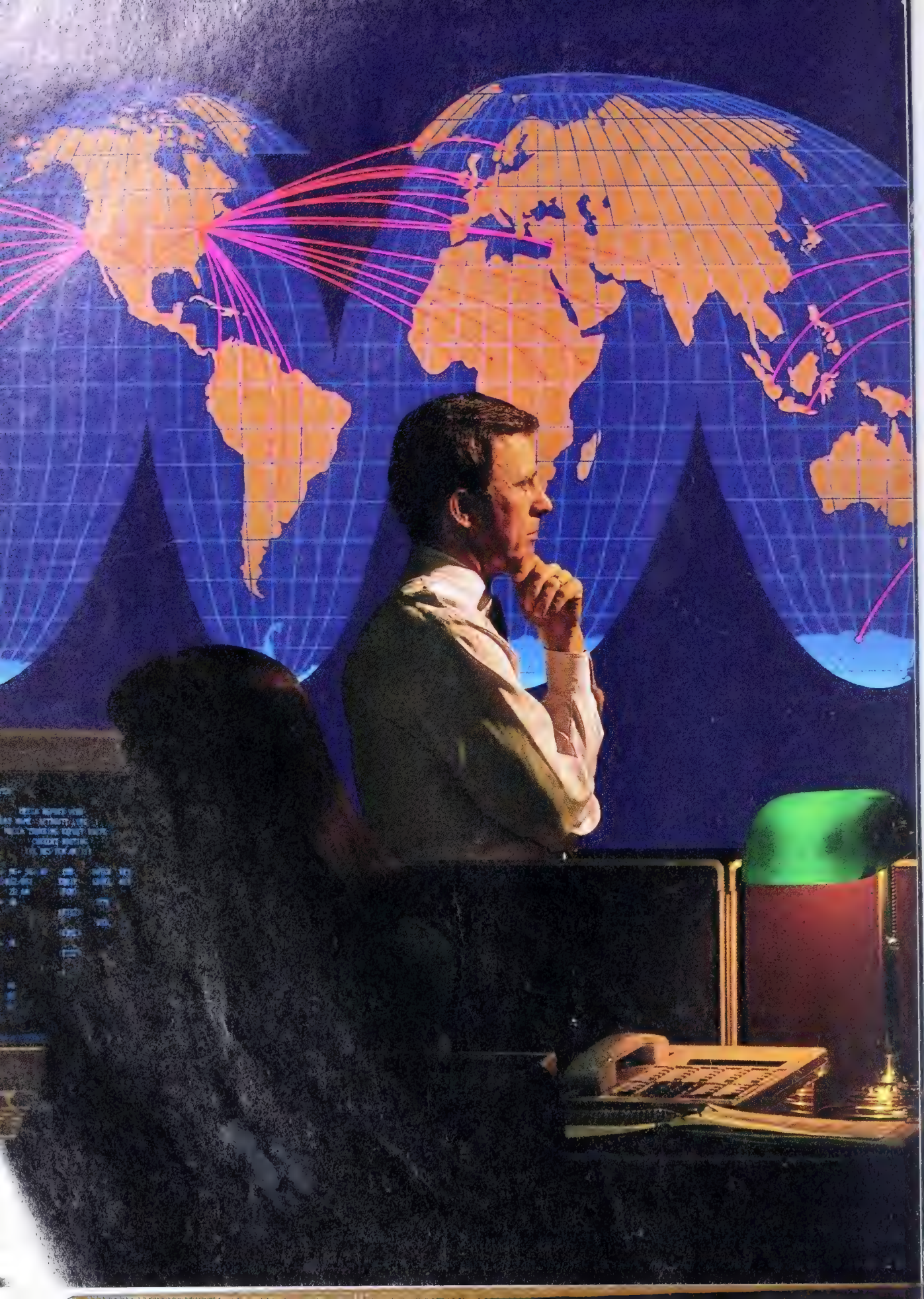
So far, however, European investors seem to be leading the way. In the past year, such companies as Germany's Siemens, France's Alcatel, and Italy's IRI have set up joint ventures in medical equipment, telecommunications switching, and air-traffic-control systems. The Finmeccanica unit of IRI is jointly producing air-traffic-control equipment with two defense electronics companies in Moscow and Leningrad.

Despite these flickers of foreign involvement, the enormity of the Soviet defense

Sverdlovsk, almost all factory workers labor in defense plants.

It's no surprise, then, that many more direct foreign investments are necessary for defense conversion to go anywhere. If done correctly, converting defense factories with Western money could be the crucial trigger for the economic turnaround of the Soviet Union. But the West must guard against the possibility that its cash ends up subsidizing unused factory lines that once again may be turning out tanks or missiles at a general's phone call.

By Rose Brady in Moscow, Igor Reichlin in Leningrad, Peter Galuszka in New York, and Amy Borrus in Washington



HOW FUJITSU HELPS MCI CHANGE THE WORLD.

MCI Communications Corporation is the long-distance telephone company that changed the world. It did it by coming up, back in the early 1970's, with a big idea. The idea was to offer long distance service that was less expensive, yet more flexible, responsive and efficient than anything that had ever been offered before.

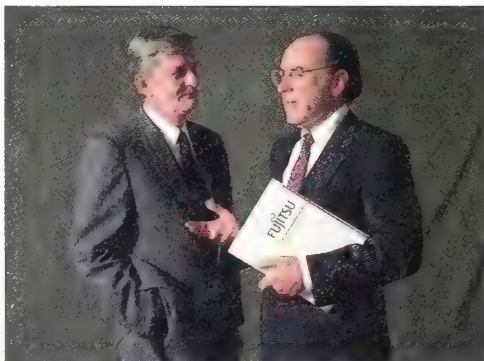
FACED ENORMOUS CHALLENGES

The company faced enormous challenges and obstacles to realizing its dream, but with great determination it succeeded. And in succeeding it changed the perception of millions of people regarding what a telecommunications company could do. It also opened up the telecommunications industry to a whole new wave of vibrant competition. And then, as country after country saw the electrifying, energizing consequences of deregulating their telecommunications industries, it expanded throughout the world. Today MCI is a giant, with a \$7 billion network—one of the most sophisticated in the world—and operations in 50 countries. And it is growing very fast.

PARTNER IN SUCCESS

MCI's partner in success, almost from the start, has been a company that has

broken through barrier after barrier in telecommunications technology, ultimately developing for MCI, and other customers, some of the most advanced lightwave fiber technology on earth—technology that has enabled MCI to leapfrog all its competitors. The name of the company is Fujitsu. It's a global powerhouse in computers and communications, a visionary force that, with 115,000 employees and operations on every continent, is leading the charge in the worldwide computer and communications revolution—changing the world wherever it goes. And helping its customers change the world, too.



Mr. Richard T. Liebhaber (right), Executive Vice President and Group Executive of MCI Communications Corporation and Paul Tobey of Fujitsu at Fujitsu's head office in Tokyo. Mr. Liebhaber says that Fujitsu's remarkable technological progress has been instrumental in MCI's success. For information call Fujitsu America, Inc. Transmission Division at 1-800-777-FAST

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KOREA THROWS OPEN ITS DOORS

From candy bars to computers, imports are suddenly welcome

For Chang In-Sook, moving back to South Korea after 20 years in the U.S. was a big letdown. Even though she earned a top salary as a gynecologist, she couldn't find consumer products that met her standards. Chang wasn't about to buy rubbery Korean beef or spend \$600 for a Korean-made designer blouse. Instead, she would fly to Hong Kong to stock up on French wine, Swiss cheeses, and high fashion at good prices. "My friends called me anti-Korean," she says.

They don't call her that anymore. Thanks to new government trade policy, she can now buy just about anything she desires in her affluent Apkujong district of Seoul. At the local Hyundai Department Store, she has her choice of imported goodies, including Mars candy bars, Whirlpool washing machines, Taiwanese bananas, and choice U.S. beef.

Chang's shopping sprees are one sign that Korea is moving to open its tightly controlled market to outsiders. Coming off a landslide victory in recent local elections, the government on July 1 gave foreigners the green light to get into Korea's retail business. Other new proposals will ease restrictions on everything from data processing to stock brokerages to airline computer-reservation systems.

ABOUT-FACE. The new program is part of an effort to beat down Korea's stubborn 12% inflation. Opening protected markets to inexpensive, high-quality imports, planners figure, should be a big help. It will also advance another important government goal: forcing Korea's powerful conglomerates, or *chaebol*, to be more competitive. Korean manufacturers can no longer count on the "forced economic patriotism" of consumers, says Park Kap-Rok, director of the Trade & Industry Ministry, who is supervising the opening of the retail market. "Today, consumers have a choice."

Korean officials also hope to appease Washington. The new policies mark a treat from a controversial government to squelch imports that triggered



PRICES OF LOCALLY MADE PRODUCTS ARE FALLING

fierce U.S. protests. Last year, Korean importers were slapped with strict new guidelines that jacked up the price of foreign goods to extraordinary levels: a General Electric Co. refrigerator selling for about \$1,600 in the U.S. cost \$4,200 in Korea. The government went so far as to send its tax inspectors to dig into the records of Koreans who bought imported cars and even those who went salmon fishing in Alaska or golfing in Hawaii.

The government has reversed a policy that sternly discouraged Koreans from buying imports

Last December, President Roh Tae-Woo began backing down, firing his Minister of Trade & Industry and transferring all officials in the ministry's U.S. trade section. A senior U.S. trade official says Korea is moving in the right direction, but "we can't say the barriers have miraculously disappeared." For one thing, the U.S. is pressing for a reduction in high tariffs on agricultural goods.

Perhaps the most significant changes are in Korea's tightly controlled financial sector. After years of failed efforts, Citibank on Jan. 1 finally received permission to enter domestic retail banking. It immediately offered 24-hour banking service—a new concept for Korea. On June 1, Citibank also got permission to open an unlimited number of branches. Merrill Lynch & Co. has the go-ahead to open a branch later this year and buy a seat on the Korean stock exchange. Next January, in another first, foreigners will be allowed to buy shares of Korean companies.

For the first time, too, Korea is letting foreign manufacturers and retailers open their own stores. Already, Ford and Christian Dior are putting out feelers on whether to open outlets. Korean officials say, and Whirlpool is set to double the number of appliances it ships to Korea this year. Japan's leading retailer, Laox, wasted no time in planning a huge discount electronics store in Seoul's posh Kangnam district, according to Korean business executives. But with an \$8 billion trade deficit with Tokyo and fears of Japan becoming too dominant, the Trade & Industry Ministry is keeping some restrictions on Japanese imports, at least until 1993.

BIG RISKS. The biggest winners are Korean consumers. Few in the growing middle class had been able to afford costly imported goods. Now, stepped-up competition is bringing prices down. Goldstar Co., the country's second-largest electronics company, has already cut prices of its camcorders and compact-disk players by about 30%. Foreign-car dealers are planning to cut markups by as much as 80%. And in a move to catch up to Citibank, Korean banks are offering round-the-clock service.

But the new program carries some big risks. With a \$4 billion trade deficit for the first five months of this year, Korea is likely to go deeper into the hole as imports rise. Some foreign executives fear that Korea might impose new barriers if the trade balance worsens. But such a move is highly unlikely, says Han Duck-Soo, director general for industrial policy at the Trade Ministry. "The genie is out of the bottle," he says. "Now we have to live with it." For Korea's consumers, at least, that should come easy.

By Larri Nakarmi in Seoul

PEACEFUL STRAWS IN THE MIDEAST WIND

An old Arab proverb goes, "take a load off my shoulders, and I'll take a load off yours." That's just what Syrian President Hafez al-Assad is doing for George Bush by giving his nod to the U.S. proposal for a Middle East peace conference leading to Arab-Israeli talks. The Syrian president is returning Bush's favors of granting him free rein in neighboring Lebanon and a significant role in the postwar Persian Gulf. Now, as Secretary of State James A. Baker III heads for his fifth tour of the Middle East, the Administration can say that it may be on the verge of achieving a breakthrough in the troubled region.

Assad has done Bush no small turn. As the 20th anniversary of Saddam Hussein's invasion of Kuwait rolls around, little of Bush's vision of the postwar Middle East has come to pass, beyond Iraq's ouster from the emirate. Saddam Hussein continues to confound the U.S. by remaining securely in power in Baghdad. The game of chicken the Iraqi leader is playing by not fully disclosing his nuclear weapons program may well lead the U.S. to resume military action.

NOTHING TO BRAG ABOUT. Bush's blueprints for keeping order in the gulf are coming up against tough obstacles. Plans to replace U.S. troops with Egyptians and Syrians are being jeopardized by the Kuwaitis' preference for Americans over Arab soldiers as well as Egypt's wanting more aid than the gulf counsels are offering. "I don't see any sign of generosity toward Egypt," said Ahmed Fakhr, a retired Egyptian major general. "It's going to rain, you have to see clouds." Liberated Kuwait is far from a showplace that Bush could point to with pride. Stonewalling on political liberalization by the ruling al-Sabahs could lead to an embarrassing confrontation



**WEST BANK SETTLEMENT:
AN OBSTACLE TO TALKS**

tion with the opposition this fall. Saddam could even exploit turmoil in Kuwait through terrorism and the network of agents the Kuwaitis say he has in the country. "The Kuwaitis haven't learned the lessons of the invasion," says Mohamed Sid Ahmed, an Egyptian analyst.

U.S. officials worry that if the momentum gained during the gulf crisis is squandered, Saddam and his radical allies in the Palestinian movement will make a comeback. Says a senior State Dept. official: "The regional players don't seem to understand that."

Many observers think such frustration could lead to a major flare-up in U.S.-Israeli relations if Prime Minister Yitzhak Shamir continues to rebuff Baker's peace proposals. Shamir fears that he can only lose by caving in on a peace conference. Shamir reasons that such a parley will be used to pressure him into making concessions to the Arabs. But the temptation is growing for Baker to use Israel's need for \$10 billion to house Russian immigrants to force Shamir to come to the party. Baker will also pressure Shamir to curb the settlement-building in the West Bank that is poisoning the chances for successful negotiations.

Despite Shamir's reluctance, there are some encouraging straws in the wind. Palestinian leaders in the occupied territories are pressing PLO Chief Yasser Arafat to bend so as to engage the Israelis. By appointing Taher al-Masri, a respected Palestinian, as Prime Minister, Jordan's King Hussein has eased the way for a joint Palestinian-Jordanian negotiating team, which the Israelis might accept. But the question is whether Bush and Baker are hungry enough for a real breakthrough to do the necessary arm-twisting.

By Bill Javetski in Washington, with Marilyn Achiron in Cairo

GLOBAL WRAPUP

JAPAN

A white paper to be released soon by economists at Japan's Economic Planning Agency comes to a startling conclusion: Japan is becoming immune to the effects of the business cycle. As the U.S. and European economies have sputtered, Japan has huddled along with 5.8% growth last year—even after a stock market crash. The paper says the fanatically efficient management of the flow of goods between suppliers and manufacturers has eliminated the inventory swings that figure big in cycles. One unbelieving Western economist, Kermit L. Schoenholtz of Salomon Brothers Asia

Ltd., predicts that growth will tumble to 2.7% in 1992.

CENTRAL AMERICA

The five chiefs of state of Central America, the onetime global hot spot, met in San Salvador on July 15 to plan the region's future. Their new strategy: to get a piece of the hemisphere's booming free-trade action by negotiating bloc trade agreements with the U.S. and other neighbors. Some of Mexico's *maquiladora* business has already moved to Guatemala and Honduras, where wages are even lower. In a conciliatory gesture, El Salvador's leftist guerrillas called a three-day ceasefire in the capital during the meeting.

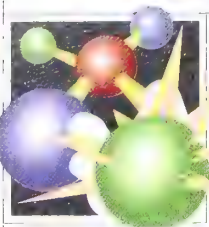
CANADA

Brian Mulroney has achieved the dubious distinction of being the West's most unpopular leader. The latest Gallup Poll reports that 68% of all Canadians—and a staggering 80% of those living in Ontario—say that the Prime Minister should resign immediately.

Much of the discontent with Mulroney can be laid to Canada's deep recession and the constitutional crisis over Quebec's special status. Mulroney is gearing up for a big, new drive to fix the constitution this fall. But it's not likely that he'll be effective at leading it.

THE NEW ALCHEMY

HOW SCIENCE IS MOLDING MOLECULES INTO MIRACLE MATERIALS



It isn't exactly *Terminator 2*, whose "mimetic polyalloy" villain melts and recomposes as it stalks its hapless victims. But in a lab in Evanston, Ill.,

a version of this Hollywood fantasy—more modest, but then it's real—is being brought to life. Using new modeling software that incorporates a wealth of knowledge from the exploding field of materials research, Gregory B. Olson, a Northwestern University professor, is designing entirely new substances, atom by atom. Olson and a group of students are hot on the trail of custom-made ceramic superconductors and ultrahigh-strength plastics, but alloys are their top priority. They already have one success, a mixture of atoms from five metals so precise that finding it by trial and error might have required "a few zillion" attempts. The resulting extra-tough steel is being tested for bearings in space-shuttle engine turbo pumps, which now must be rebuilt after every flight.

Materials have always influenced the basic fabric of life. The Stone, Bronze, and Iron Ages marked key periods when humans fashioned materials into new tools that vastly improved their lot. So it is with the latest—and most sweeping—revolution in materials science. Using ultraprecise new technologies, researchers are probing worlds far tinier than the submicroscopic realm of viruses. Like voyeurs peeping into a particularly raucous party, they are peering into the world of atoms and unlocking the secrets of how they interact. Then, using technology developed primarily to deal with the rapidly decreasing dimensions of microelectronics, modern-day alchemists are rearranging molecules—and even atoms—to assemble novel substances from scratch.

Often, the most commercial results of this wizardry are, like Olson's steel, offshoots of existing materials. But researchers are also probing the unknown.

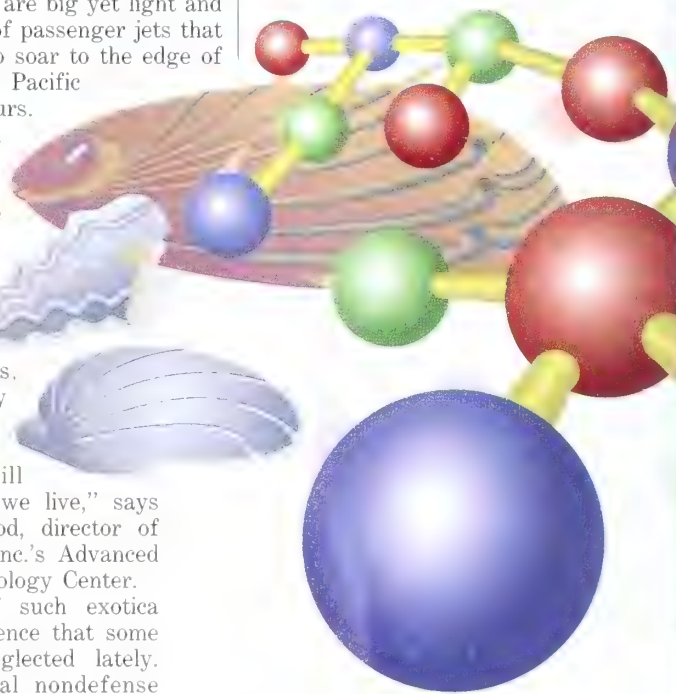
They're making "aerogels," airy silicon concoctions that far outperform the best insulators; ceramics pliable enough for use in car or jet engines; and composites embedded with artificial "nerves" and "muscles" that let them respond to stress almost as a living thing would. With such substances in mind, scientists dream of cars that are big yet light and fuel-efficient, and of passenger jets that are light enough to soar to the edge of space and hop the Pacific in a couple of hours.

In the \$300 billion electronics industry, new materials are pushing the speed of chips and computers to the edge of physical limits.

These advances, leading eventually to products such as handheld supercomputers, will "change the way we live," says Harry F. Lockwood, director of GTE Laboratories Inc.'s Advanced Components Technology Center.

The promise of such exotica should boost a science that some say has been neglected lately. Since 1980, federal nondefense support for materials R&D has fallen 17% in real dollars. Industry support has plummeted, too, experts add, while Germany and Japan, among others, are pumping money into the field. A 1989 report by the National Research Council found that America's competitive position in metals and ceramics is declining vis-à-vis Japan's and that Germany and Britain have caught up. To stay in the game, says the Materials Research Society, a trade group, U.S. government and industry need to add \$1.25 billion to the \$3 billion a year they now spend on materials R&D.

Confronted with losing ground in a \$148 billion world market, the usually laissez-faire Bush Administration seems abnormally concerned. In April, David L. Huber, acting executive director of the National Critical Materials Council, announced an Administration materials-research initiative. The White House



BIOMIMETICS

Nature provides the molecular architecture for some of the most interesting new materials. The abalone shell is an excellent example of a ceramic composite made mainly from a simple material—chalk. Its relatively high strength comes from the unique way in which its mole-

cules are arranged, in a brick-and-mortar pattern with a natural polymer as the glue between the 'bricks.' Using higher-tech materials but enlisting the abalone as a model, researchers have synthesized an impervious tank armor that is twice as tough as any man-made ceramic and more effective than today's arm-

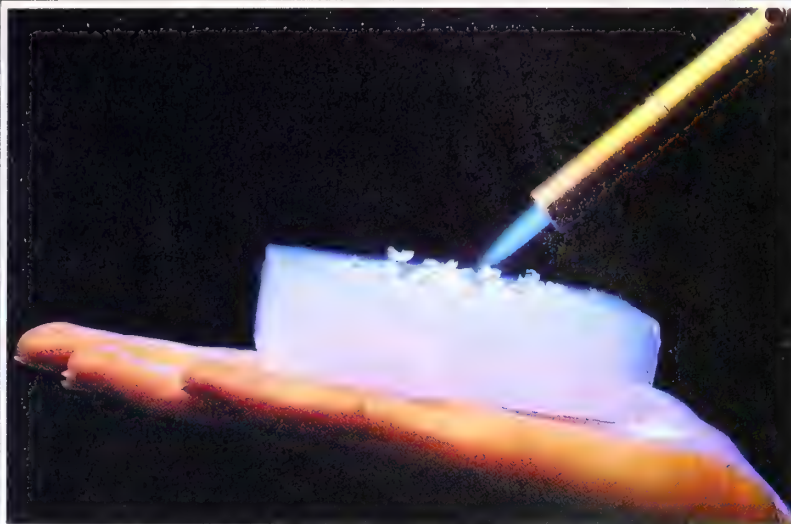
Office of Science & Technology Policy, with which Huber's group is affiliated, wants to add hundreds of millions in money and reprogrammed dollars for materials research, probably in the 1993 federal budget. Huber wants to open R&D priorities: it's not clear that we're doing all we should with the money we have," he says.

He is trying to re-ignite a movement whose roots reach back to the 1960s, when researchers began large-scale production of molecules that nature overlooked. The result was an explosion in synthetics that revolutionized industries such as packaging, homebuilding, and textiles. Today, athletes use carbon-fiber-reinforced golf clubs, polypropylene sweatbands that draw sweat away from the body, and waterproof jackets that breathe. Scientists know so much about how the chemical structure of a polymer—a chain of repeating molecules—dictates its function that researchers can sit down at computers and juggle together materials with the de-

sired qualities. This means that "instead of 10-year development cycles" for finished products, "we'll see results in 3 to 5 years," says Donald P. Knechtges, vice-president for marketing at B.F. Goodrich Co.'s Geon Div. in Cleveland.

The most dramatic advances have come in electronics (page 54). To meet the increasing demand for improved performance in storing and processing data, researchers are working harder than ever on techniques and equipment to shrink silicon circuitry. One of the newest tools is the scanning-tunneling microscope, a machine that uncovers incredibly accurate information about the

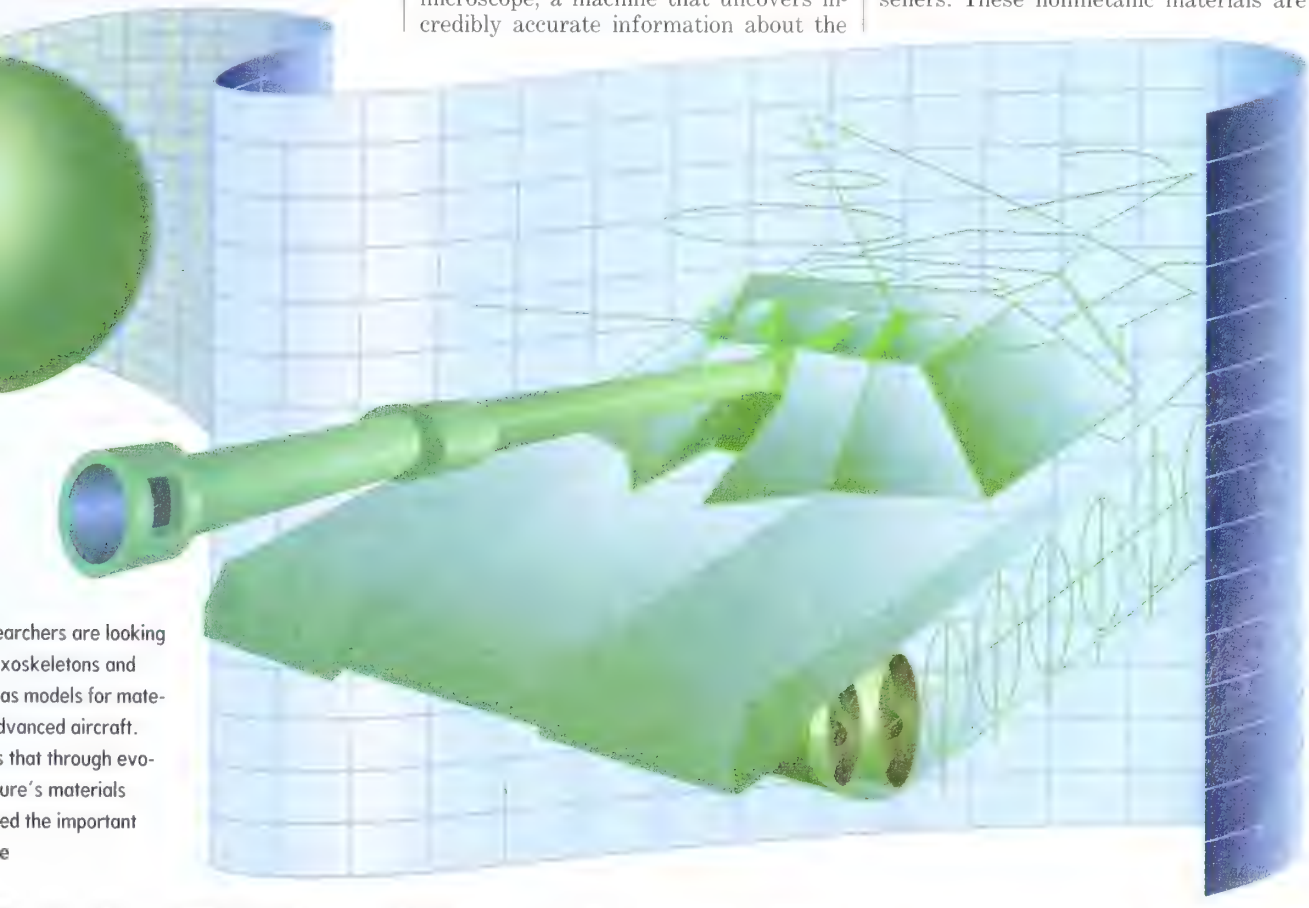
positions of individual atoms on surfaces. Couple the STM with advances in computer modeling, and "we can model how molecules place themselves on a substrate without doing exhaustive hunt-and-peck experiments," says Frank Fradin, associate director of physical sciences at Argonne National Laboratory, near Chicago. Now, scientists are using these same tools and insights to fashion materials to improve everything from planes to bridges to artificial body parts.



SMOKE SCREEN: SUPERLIGHT AEROGELS MAKE EXCELLENT INSULATORS

ENGINEERED MATERIALS These alchemists follow a less greedy pursuit than the Merlins of old, who sought to turn lead into gold. In its most practical form, the new alchemy seeks to devise better versions of structural materials—the metals, composites, and ceramics that permeate everyday life. A modest-sounding endeavor, it's nonetheless likely to produce vast riches. In a decade, Japanese industry alone expects to be using \$90 billion a year worth of such products.

Ceramics will be one of the hottest sellers. These nonmetallic materials are



Researchers are looking at molecular skeletons and using them as models for materials for advanced aircraft. They believe that through evolution, nature's materials have revealed the important secrets of the universe.

ENGINEERED MATERIALS

These are variations on the metals, plastics, composites, and ceramics that already are used in large quantities in industries as diverse as aero-

space, autos, and construction. Now, scientists are engineering into these materials such high-performance properties as increased strength and stiffness, lighter weight, and higher temperature resistance. Some exam-

ples include superstrong, corrosion-resistant alloys and flexible ceramics that can be molded into engine parts. Improved structural materials hold the greatest promise for near-term profits

superstrong and can withstand extreme heat, holding out the promise of hotter burning, more efficient engines needed for jets and low-polluting cars. But ceramics are brittle, which limits their use. Now, by adding small amounts of polymers or fiber "whiskers," researchers are developing much more ductile varieties. "If you can remove their deficiencies, you can open ceramics to a wide, wide range of applications," says Richard W. Siegel, an Argonne researcher. That could include everything from lighter, more durable engine parts to flexible superconducting wire and tougher cutting tools.

Metal alloys are getting a face-lift, too. For instance, a 15-year, \$6 billion initiative jointly funded by the U.S. defense agencies, NASA, and seven jet-engine makers aims to double the thrust of aircraft engines by the year 2003 without increasing their size or weight. "Today's titanium alloys and nickel alloys don't have the necessary strength or temperature capabilities, and they're too heavy," says James S. Petty, manager for the project at Wright Paterson Air Force Base in Dayton, Ohio. But by using new alloys, Petty's team is nearing its first-step goal of a 30% increase in the ratio of engine thrust to weight, plus a 20% gain in fuel efficiency. These improvements will show up in the new stealth fighter's engines, to be built by Pratt & Whitney.

One obstacle has been finding key engine-parts materials that can withstand temperatures of up to 800F,

the point at which more of the oxygen entering an engine combines with fuel, creating greater efficiency. Titanium, a traditional jet-engine metal, will burn up at that temperature, says Petty. So, his researchers are looking to so-called intermetallics—mixtures that go beyond chemical bonding by intertwining differing atoms within the same crystal structure. Made of titanium and aluminum, or of nickel and aluminum, intermetallics are superlight and can withstand temperatures up to 1,400F. Adding ceramic fibers to these creates composites that are three times as strong, by weight, as current alloys used in jet engines, Petty adds.

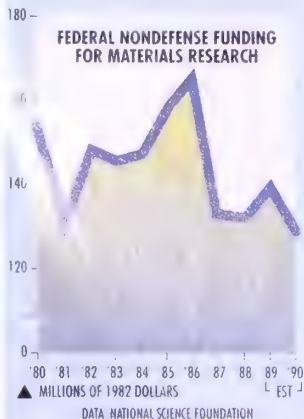
ATOMSCOPIC MATERIALS Improved structural materials may be the most practical products of the new research. But, not content with mere variations, the most aggressive new alchemists are flirting with creation—developing entire new classes of materials. These will foster big advances in electronics and elsewhere. Argonne's Siegel, for example, is forming clusters of atoms, called crystalline grains, into superdense ceramics or metals. In these "nanophase materials," each crystal is less than 100 nanometers, or billionths of a meter, across. That is smaller than most viruses.

The individual grains of most metals or ceramics consist of millions of billions of atoms. But the grains that make up nanophase materials contain just a few thousand. After these grains are squeezed, under pressure, into a solid material, they exhibit remarkable properties. Siegel's superdense ceramics can be bent and molded like plastics and extruded or formed into a final shape without the shrinkage normally typical of ceramics. Nanophase versions of metals such as copper or palladium are five times as strong as their larger-grained counterparts. Siegel is also fashioning nanophase composites—combining tiny crystals of ceramics with metals—and he is working on forming unusual metallic alloys. "There are astounding opportunities," he says.

Scientists aren't sure why nanophase materials act as they do, but Siegel says that the size of the crystalline grains plays a big role. Nanophase metals, for example, are so strong because it requires a lot of energy to force cracks among the close-knit grains. For research purposes, Siegel's group usually makes only penny-size disks of nanophase materials. But, he says, "there's nothing in the process that prevents it from being scaled up." In late 1989, in fact, Siegel helped found a company to commercialize the Argonne work. Called Nanophase Technologies Corp., it is making up to several grams of the materials per hour. "I suspect within a year we'll be at the kilogram-per-hour stage," he says. The first use for nanophase

WANING SUPPORT FOR NEW MATERIALS

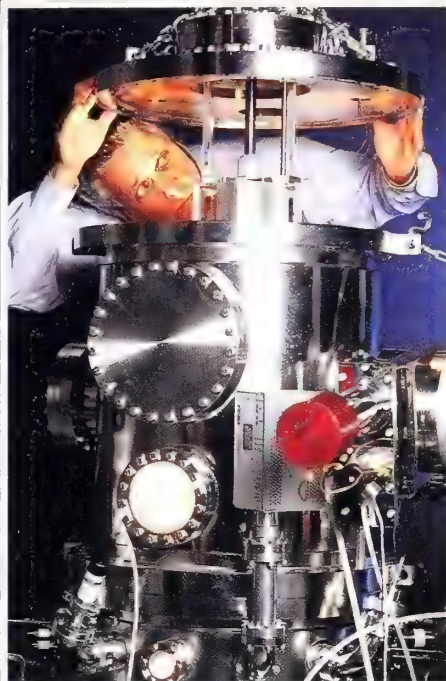
FEDERAL NONDEFENSE FUNDING FOR MATERIALS RESEARCH



materials will be in electronics—ceramic capacitors and optical devices—and in making catalysts to drive chemical reactions.

The Japanese, meanwhile, are hot on the trail of designer compounds called functionally gradient materials (FGMs). These combos of ordinarily incompatible materials—metal and ceramics—remain viable over perhaps a 1,000-degree range in temperature and withstand searing heat—more than 3,000F. That would make them useful for everything from engine space planes to making turbine blades for nuclear power plants. Researchers have known that a “sandwich” of metals and ceramics could provide unequal heat resistance and elasticity. But the sandwich usually peels apart under thermal or mechanical stress.

To avoid that, the Japanese use techniques with names such as chemical vapor deposition and particle injection to lay down multiple, ultrathin layers that gradually transform a material from 100% metal to a 50-50 mixture to 100% ceramic. This eliminates the sharp boundary where the ceramic ends and the metal begins. So, the new material sticks together. Japan's Science & Technology Agency first advanced the notion of FGMs as a basic research project in 1986. Already, steelmakers NKK and Nippon Steel have taken up the challenge, as has Toshiba Ceramics. “If it is a good idea, money flows in that direction,” says Toshikazu Ishii, deputy director of MIT's office of material science and technology.



IN ARGONNE'S NANOPHASE LAB: CERAMICS THAT BEND AND SUPERSTRONG METALS

SMART MATERIALS As impressive as all this sounds, for some engineers the new alchemy implies the metaphysical. They want to impart the ultimate property: a crude sort of intelligence that infuses materials with artificial “nerves” and “muscles.” Because these altered ceramics and composites sense changes in their environment and then react accordingly, they are called smart materials.

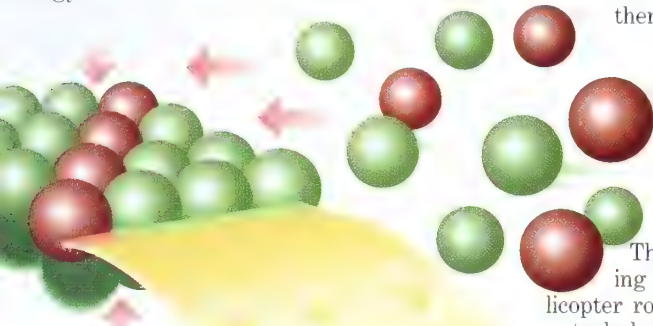
At Michigan State University, for example, Mukesh V. Gandhi and Brian Thompson are working on an adaptive helicopter rotor that can sense turbulence and stiffen in response. The Air Force is sponsoring work on

a smart ceramic for the leading edge of airplane wings: It would adjust its shape to achieve maximum lift under changing conditions and thus improve fuel efficiency and safety. And Robert E. Newnham, professor of solid state science at Pennsylvania State University, is developing a “stealthy” material for submarine hulls that flexes to change shape and reduce underwater turbulence. That would help a sub escape detection by underwater listening systems.

One key to making materials “smart” is to imbue them with nonmechanical materials that change their shape or physical state without using moving parts. Electro-rheological fluids are one such family: They change from a liquid to a solid milliseconds after a small electric current is applied. By scattering these fluids throughout a ceramic, Gandhi and Thompson can dampen vibration in their rotor. Sensors on the outside of it pick up damage or turbulence, then send a signal to stiffen the rotor blades.

In a variation on this concept, Craig A. Rogers, director of Virginia Polytechnic Institute's Center for Intelligent Materials Systems & Structures, adds wires of nickel-titanium alloy to the graphite-reinforced composites used in everything from aircraft to tennis rackets. The nickel-titanium alloy is one of a family of so-called shape-memory metals—they remember their shape when heated. Rogers says that normally, graphite-reinforced epoxy loses half its stiffness when the temperature goes over 300F—not a pleasant prospect in a high-performance airplane wing. But “with the memory fibers, the graphite epoxy increases its stiffness at the higher temperatures,” he says. When heated, as in flight, the fibers try to return to their remembered shape, adding energy to the material. The resulting composite is more than 10 times as stiff at high temperatures as those used in aircraft now.

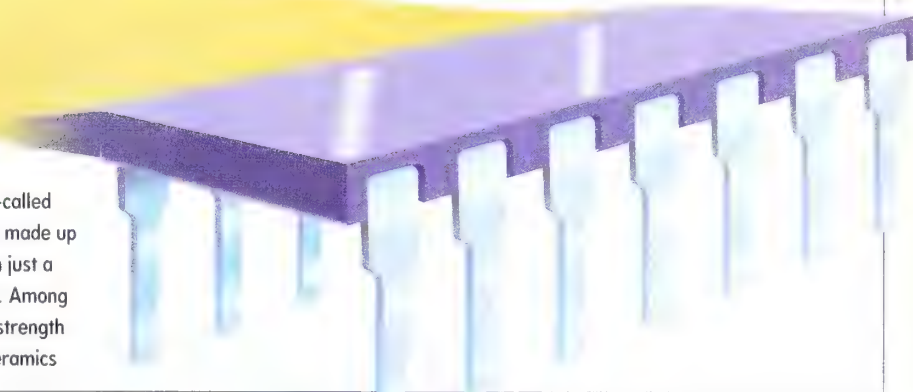
BIOMIMETICS Attempts to imitate life are at the foundation, too, of biomimetics, perhaps the most revolutionary new materials approach. For this, scientists look to nature for inspiration, to materials as



ATOMSCOPIC MATERIALS

Using techniques developed in the race to make smaller, faster semiconductors, scientists are rearranging atoms to novel substances. By laying thin films of different elements—some just an atom or two thick—researchers can design in superconductivity or high strength. They also

are working with so-called nanophase materials made up of grains that contain just a few thousand atoms. Among the results are high-strength metals and pliable ceramics



model as abalone shell, sharkskin, and insect exoskeletons. They start from the view that Mother Nature offers the supreme models: "As far as we know, her failures are extinct," says Lieutenant Colonel George A. Haritos, associate director of the Air Force Office of Scientific Research (AFOSR). "We are mimicking the best she can offer."

For instance, Ilhan A. Askay, professor of materials science and engineering at the University of Washington, was intrigued by the shell of the abalone—a flattened, ear-shaped mollusk shell made from calcium carbonate, or common chalk—that is hard to break even if a

breathe through it, insulates it, and provides all kinds of sensing devices." A multifunctional skin that removes heat and senses damage would be particularly useful for the aerospace plane.

The exoskeleton is also resilient. "It is designed to absorb enormous amounts of energy in relative terms before it breaks down," says Haritos. Such a quality is important because one of the biggest barriers to using composite materials in aircraft wings is concern that the composite will fail catastrophically after suffering limited damage. In the beetle, nature has designed in damage control. Conventional composites are re-

implicated in the destruction of the ozone layer. A Swedish company, Airglass, is trying to drum up interest in using them in insulated windows.

These and other discoveries may mark the 90s as the golden age for materials science. With new federal support, the U.S. could regain some of its edge. But money is just part of the equation, says Argonne's Fradin. In Japan, companies, not academic or government labs, form the cutting edge: Nearly 75% of funding for materials work in Japan comes from industry, vs. half in the U.S.

The challenge, in short, is to envision products from promising technologies

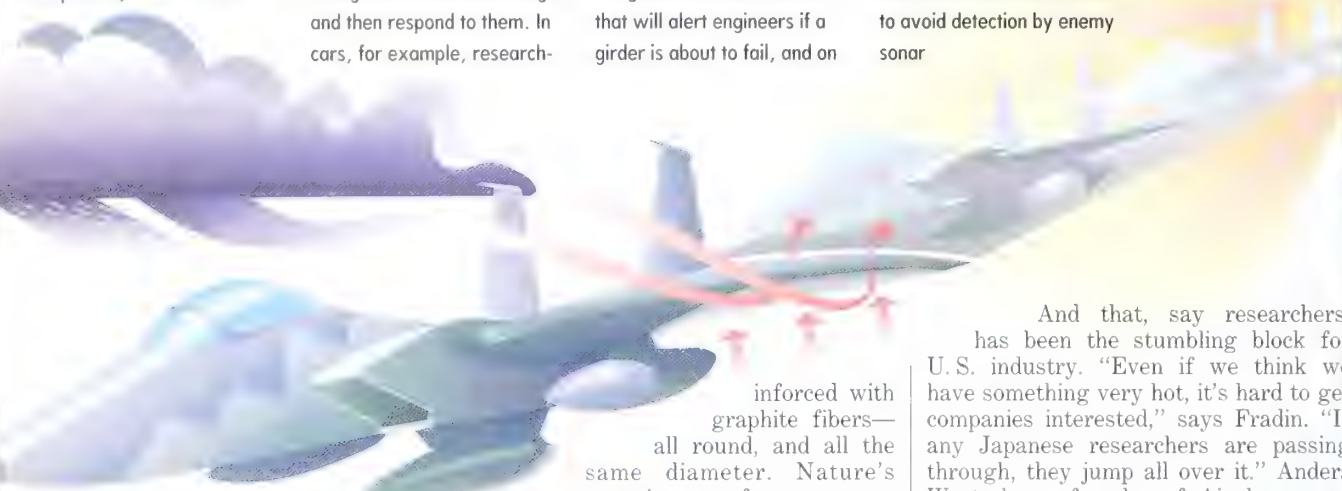
SMART MATERIALS

Usually metals, ceramics, or composites, these are embed-

ded with sensors and actuators that give them some of the characteristics of living things. They can sense changes in their surroundings and then respond to them. In cars, for example, research-

ers have already developed smart suspension systems that dampen vibration. They are also working on smart bridges laden with sensors that will alert engineers if a girder is about to fail, and on

helicopter rotors that stiffen in response to turbulence. The military envisions smart submarine hulls that can alter their acoustic characteristics to avoid detection by enemy sonar



300-lb. beachcomber steps on it.

When viewed under an electron microscope, the shell represented a near-perfect imitation, so to speak, of a ceramic composite. Using higher-tech materials but enlisting the abalone as a model for arranging the molecules, Askay has synthesized an impact-resistant tank armor that's twice as tough as the man-made ceramics now used. The U.S. Army is testing his armor at Lawrence Livermore National Laboratory in California.

One of the systems AFOSR researcher Fred L. Hedberg sees benefiting from biomimetics is the proposed national aerospace plane, which would enter low orbit during its two-hour trip from New York to Tokyo. It would carry a much greater load than the space shuttle, but to reach the right speed and altitude, it must weigh less. That's where biomimetics comes in, says Hedberg, who has studied the strong yet lightweight exoskeleton of the horned beetle. "When nature builds a protective coating for an insect, it also permits the animal to

be reinforced with graphite fibers—all round, and all the same diameter. Nature's composites are far more complex, made from intertwining fibers that often themselves are composites. And the fibers vary in shape from round to extreme oval. "This complex structure is something man is just now experimenting with," says Haritos. "But it is the wave of the future."

With an explosion in the number of new materials coming out of labs, it isn't clear yet what all the uses might be. Take carbon 60—a new form of carbon synthesized in bulk just two years ago. The 60 carbon atoms of this substance are organized in a soccer-ball shape reminiscent of R. Buckminster Fuller's geodesic domes. Called "buckyballs," they may be used for lubricants, high-temperature superconductors, or as the foundation for new plastics. Aerogels, developed at Lawrence Livermore last year, have enormous potential. Often called "frozen smoke," they incorporate superior insulating abilities in one of the world's lightest known solids. Livermore researchers envision them replacing foam insulation, whose manufacture is

And that, say researchers, has been the stumbling block for U.S. industry. "Even if we think we have something very hot, it's hard to get companies interested," says Fradin. "If any Japanese researchers are passing through, they jump all over it." Anders Westerberg, founder of Airglass, says the U.S. and European companies he has approached in search of \$7 million for a commercial-scale aerogel plant have held back, concerned about how long it will take to turn a profit. But four or five Japanese companies are interested. And "when I tell them it will take several years to see any kind of payback, they say that's O.K."

Ultimately, the impact of designer materials research will be strikingly evident in the world around us. Faster trains, stronger buildings, and more lifelike artificial limbs will all carry the mark of the modern-day alchemist. New materials will also play an integral role in solving some of society's most pressing problems, from cleaning up the environment to reducing energy consumption. All in all, it's an even better goal than transforming lead into gold.

By Naomi Freundlich in New York, with Neil Gross in Tokyo, John Carey in Washington, and Robert D. Hof in San Francisco

Continued on page 54



Subaru Legacy LS Wagon

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CREATING CHIPS AN ATOM AT A TIME

Tiny 'nanosandwiches' grown in crystals will put a supercomputer's power in the palm of your hand



Visitors to Praveen Chaudhari's lab used to stop in their tracks, perplexed by the scene before them: Candles gleamed alongside the exotic equipment used to explore materials and structures for tomorrow's chips. "People would think we were praying," muses Chaudhari, a senior IBM scientist. But the candles had a down-to-earth purpose. His team was experimenting with semiconductor wires so tiny that the friction of a person moving through the air generated enough static electricity to zap the circuits. The candles solved that. Soot particles from their flames discharged the air, protecting the "nanoelectronic" devices.

Nanoelectronics is the watchword of the coming revolution in semiconductors. Chipmakers are entering a realm where transistors will be too tiny to "print" on silicon. Instead, they'll be "grown" in the material, as clusters of atoms. These devices will be measured in nanometers, or billionths of a meter. A fat human hair is 10,000 nanometers in diameter. The wires Chaudhari worked on a decade ago were 10 nanometers wide.

BIG LEAP. Today, at key research centers in the U.S., Japan, and Europe, scientists are thinking even smaller. They talk in angstroms, or tenths of a nanometer, and they're making materials and devices by piling up elements in layers as thin as two angstroms—just a single atom thick. Tinier transistors can be packed more closely, which means more powerful circuits that run faster. So, when these technologies are perfected, they'll bring quantum

leaps in performance to all things that use chips, from computers and cars to satellites and appliances. A shirt-pocket supercomputer may be in the cards, as well as memory chips that hold a library.

The industry is going all out to make this happen. For the first 25 years after the integrated circuit was invented in 1959, the number of transistors per chip doubled every other year. Had auto makers done as well, "a Rolls-Royce would cost \$3 and get 100 million miles to the gallon," jokes George H. Heilmeier, president of Bell Communications Research Inc. (Bellcore). Since 1985, though, the growth rate for transistor counts has slipped a bit, according to market watcher Dataquest Inc., and it's headed lower. So chipmakers are turning to basic physics to keep the shrinking act going for another 25 years.

Today's chip technology is based on bulk materials: The thinnest wires on the fastest chips are thousands of atoms

across. But the day is coming—three chip generations from now—when bulk properties won't be able to cut it. The first dynamic random-access memories (DRAMs) of the next century won't be feasible without big breakthroughs. The reason: Below dimensions of 0.2 microns or 200 nanometers, conventional transistors will be too minuscule to offset the dire effects of "quantum tunneling." A phenomenon of quantum physics, tunneling occurs when electrons squirt right through solid matter and electrical barriers that, in bulk materials, are usually impassable. A 100-nanometer transistor would leak so many electrons when switched off, and release so few when turned on, that it wouldn't be reliable.

"We are moving into a size range where we have to reexplore the physics involved in semiconductor devices," says Richard D. Skinner, president of consultant Integrated Circuit Engineering Corp. And that means devising technologies to harness quantum mechanics.

Quantum transistors will be so tiny as to verge on the ethereal. And their switching speeds would, in theory, be 1,000 times as fast as anything around now. Building such critters, says Arno A. Penzias, vice-president for research at AT&T Bell Laboratories, will require radically new production methods that can "create semiconductor structures atom by atom." How this might be done in factories is anyone's guess. But the tools will have to be very precise. G. Dan Hutcheson, president of

consultant VLSI Research Inc., notes that in quantum electronics, "a variation of just one or two atoms can make a drastic difference." In fact, Bell Labs has found that clusters of 13 silicon atoms behave so differently from clusters of



IBM researcher Praveen Chaudhari burns candles in his lab to clear from the air traces of static electricity that could zap his nanoelectronic devices

other size that "Silicon-13" is almost distinct element. "We're still trying to find out why," says Mark Jarrold, a Bell Labs researcher.

A technique called band-gap engineering looks like the best way to harness quantum electronics. Band gap is physicspeak for the energy difference, or gap, that separates the electrons in an atom's outermost orbit, or band, from those in the next lower band. So, the band gap is the amount of energy that an electron must absorb to make a quantum jump to the highest orbit, where it's in a position to conduct electrical signals.

ENDING OOMPH. Electrons by nature prefer to occupy the lowest possible energy band. So, scientists theorized, electron tunneling could be regulated by exploiting this tendency. The idea is to sandwich an ultrathin layer of a relatively good conductor between another material that's not so hot: gallium arsenide, for example, between sheets of gallium aluminum arsenide. The good conductor's outermost electrons have less energy than those orbiting the other compound's atoms. As a result, the inner layer's electrons are trapped, unable to muster enough oomph to muscle past the high-energy electrons of the surrounding materials—unless outside energy, such as a switching signal, is applied.

Scientists dubbed such hypothetical structures "quantum wells" and started working for them in the 1960s, spearheaded by Bell Labs and IBM. But before they could slap nanosandwiches together, they had to identify the best pairings of materials and develop new methods for laying down ultrathin films. Finding the right recipes is critical because a chip must be a perfect crystal. When two elements are combined, each material's crystalline lattice, or arrangement of atoms, must match up exactly. Otherwise, the composite crystal's "superlattice" will contain structural flaws that can render a chip useless.

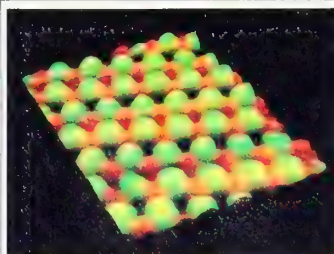
Keeping tight reins on crystal growth requires some of the most sophisticated machinery ever built. Take molecular-beam epitaxy (MBE). An MBE system creates the highest vacuum on earth. That's so molecules of air won't affect the atoms ejected by a sophisticated spray gun that it is so precise it can paint wafers with successive coats of material that may be no more than a single atom thick. While the U.S. pioneered such techniques, Japan's consumer electronics engineers are now

at the cutting edge of some equipment. Fujitsu Laboratories Ltd., for instance, is experimenting with an innovative pulse-jet epitaxy (PJE) system that can produce gallium-based superlattice crystals with superior electrical properties.

Still, it was a U.S. team that finally turned a quantum well into the first working quantum transistor. In the summer of 1988, Texas Instruments Inc. researchers led by Robert T. Bate discovered how to make a quantum well switch on and off. The trick is tickling the middle layer with a current of just the right voltage while pulsing it at just the right frequency. Suddenly, the band-gap barriers topple, and electrons zip across the inner layer—so fast that it's hard to measure the transistor's switching speed. Roughly, it's 5 femtoseconds, or quadrillionths of a second. By comparison, it takes light, traveling at 186,000 miles per second, some 200 femtoseconds to traverse the period at the end of this sentence.

More recently, these tools and techniques have yielded what may be the biggest breakthrough yet: silicon-based materials with features similar to those of gallium arsenide, once considered the chip material of the future. That wasn't supposed to happen. Band-gap engineering is possible only in semiconductors made from two materials, and they must be essentially identical crystals. Silicon's nearest cousin is germanium—not a close match. But nearly a decade ago, Bernard S. Meyerson, an IBM physicist, decided to give it a whirl. "Rule No. 1 in this business is never bet on what somebody can't do," he says. What he found is that silicon alloys containing 5% to 10% germanium are sufficiently elastic to grow into defect-free crystals. "By getting the dimensional control down to the atomic level," says Meyerson, "you can do pretty amazing things."

The first transistors fabricated with Meyerson's hybrid clocked in more than a year ago with a switching speed of 75 gigahertz, or 75 billion on/off cycles per second. That's nearly double silicon's previous record of 40 gigahertz



SEEING ATOMS

Scientists got their first clear look at individual atoms—shown here in a germanium semiconductor crystal—after IBM invented the scanning-tunneling microscope

and far above the 45-gigahertz level where silicon was supposed to top out. Switching speeds continue to improve, though Meyerson won't say by how much. But even the initial mark provides so much new latitude that gallium arsenide may never replace silicon, declares John A. Armstrong, IBM's vice-president for science and technology. For chipmakers, that's sweet music. Changing over

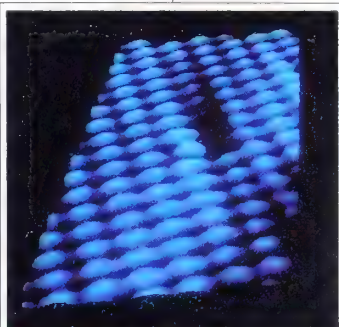
to gallium arsenide would cost a bundle and mean that three decades of know-how would get scrapped.

Every major chipmaker has now launched silicon-germanium projects. Still, researchers have barely dented the mix of technologies needed to build quantum-effect chips. Today's chief challenge is to find a way of connecting thousands of quantum transistors in an integrated circuit. Printed-metal connections won't do. Even if the wires could be slimmed down vastly, they might melt, since resistance in metal conductors rises rapidly as size diminishes.

WISPY LINES. So, researchers are looking to band-gap engineering to fashion quantum wires. Scientists at Tokyo Institute of Technology and Stuttgart University use pinpoint beams of electrons or ions to scribe wispy lines in semiconductors. Then, a better conductor is deposited in the channel and masked with the original material. That's how Bellcore produced the first quantum-wire laser last year. Its gallium arsenide core had a cross-section only 30 atoms high by 300 atoms wide. Yet many scientists consider that too bulky. Learning to grow finer quantum wires in the crystal, along with quantum transistors, is one focus of research at facilities such as the Center for Quantized Electronic Structures, established in 1989 at the University of California at Santa Barbara. And Japan's Ministry of International Trade & Industry is launching a 10-year nanotech initiative that it hopes will be supported by dozens of companies to the tune of \$100 million or more.

When it all comes together, the wonders of nanoelectronics should dwarf today's digital marvels. "Because we are learning how atoms carry on and how that affects properties," says Simon Ramo, retired co-founder of TRW Inc., computers and other high-tech gadgets will no longer be limited by nature's materials. And chipmakers may soon make their wildest material dreams come true.

By Otis Port in New York



SPOTTING DEFECTS

Imperfections in a semiconductor crystal, such as the atoms missing at center, can be 'circuit killers.' A printed 'wire' wouldn't bridge the gap, so the chip wouldn't work

THE PLUS IS DOS/MAC COMPATIBILITY.

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Kodak Ektaplug 7016 printer



Developments to Watch

EDITED BY NAOMI FREUNDLICH

THE VAMPIRE BAT: NATURE'S OWN CLOT-BUSTER?



The vampire bat's sinister reputation could soon change, as scientists at Merck Sharp & Dohme study ways to use a clot-dissolving molecule in its saliva to treat heart disease. Vampire bats depend on a diet of fresh blood. To make sure they get a full meal from their victims, they release a plasminogen-activator called Bat-PA

that prevents blood from clotting and closing the open wound. Many hospitals use human-tissue plasminogen-activator (tPA) to dissolve blood clots in coronary arteries and halt heart attacks, but the therapy has drawbacks. tPA must be administered early on during a heart attack, and it's difficult to achieve the high levels needed in the bloodstream because tPA is cleared out very rapidly. In rabbit studies, Bat-PA opened blocked arteries twice as fast as tPA and stayed in the bloodstream four times as long. Merck scientists are testing Bat-PA in primates but won't say when human testing will begin.

JUMP UP YOUR MITT— IT'S TIME TO PLAY BALL

Boston Celtics rookie Dee Brown wowed basketball fans earlier this year when he pumped up his Reebok sneakers on national television before going on to win the National Basketball Assn.'s slam-dunk competition. Now, the idea is leading to other sports. On July 16, Reebok announced that it will jointly develop Pump technology for ice skates and roller skates made under Sport Maska Inc.'s CCM brand. And Coppee (Mass.) manufacturer Spalding Sports Worldwide has unveiled a newly designed leather baseball glove featuring a multichambered polyurethane air bladder sewn into the back. A pump button on the thumb of the glove will allow the wearer to customize its fit. The new glove, which will be available in both baseball and softball sizes, also features ridges in the palm and back that the designers say will greatly increase its flexibility and performance.

Spalding plans to have its new product—which, at \$120, will cost four times the cost of the average mitt—out in time for the 1992 baseball season. And Sport Maska says it plans to have all players using the Pump skates by the fall of 1992.

CRACKING THE DREADED ALZHEIMER'S IN MICE AND MEN

Scientists know that the brains of Alzheimer's-disease victims are full of tangled clumps made from a substance known as amyloid beta protein. What they don't know is whether the protein deposits cause the deadly brain degeneration or are merely a symptom. Now, in two separate studies, researchers at Miles Research Center in West Haven, Conn., and California Biotechnology Inc. in Mountain View are nearing an answer.

Both groups used mice that were genetically engineered to make extra amounts of the protein. What they found was that rather than being broken down by the body, the extra protein accumulated in the brains of 12- to 15-month-old mice much as it does in human victims of Alzheimer's. The Miles team reported in the July 19 issue of the journal *Science* that the accumulation didn't begin until the animals were six months old, suggesting that damage increases with age, just as in human Alzheimer's. The next and crucial step: letting the animals live a year or two longer to see if brain cells die. If so, scientists could then tackle the cruel disease by throwing a wrench into the genetic machinery that makes the protein.

IN CHICAGO, 'SMART CARS' MAY SOON LOOP THE LOOP

Massive construction on nearly every major Chicago highway could mean traffic jams for several years to come. So Motorola Inc. and its partners have an ideal location to launch the most ambitious field test yet of "smart cars" and "smart highways." With the financial backing of the U.S. and Illinois Transportation Depts. and several state universities, the company is spearheading a five-year, \$40 million experiment to reduce traffic congestion and shorten travel times.

The project, called ADVANCE (for Advanced Driver & Vehicle Advisory Navigation Concept), calls for equipping up to 5,000 vehicles with in-car navigation systems starting in 1993. Global positioning system (GPS) satellites will help drivers pinpoint their precise location while a state-run traffic center relays up-to-date traffic information to the car via radio waves. On a screen attached to the dashboard, the system will use the data to plot and display the least-congested, fastest route to the driver's destination. It will also give directions in a synthesized voice. Motorola will develop both the in-car systems and the communications network for the traffic center.

A BIG SETBACK FOR 'LITTLE SCIENCE'

Last year's federal budget calls for ceilings on discretionary spending that make it impossible to pay for planned increases in Big Science projects such as the Superconducting Supercollider (SSC) without cutting back on "little science." In voting for President Bush's requested \$2 billion for the space station in fiscal 1992, for example, the



House dramatically sliced NASA's smaller science missions.

But this year's squeeze is tiny compared with what's to come, warns a new study by the nonpartisan Congressional Budget Office. If the Administration's three biggest projects—the space station, SSC, and NASA's Earth Observing System—proceed on schedule, their bite of all domestic discretionary spending would reach 2.8%—a "breathtaking" \$6 billion—by 1996, says CBO analyst Philip Webre. Unless the unlikely occurs—say, federal R&D funding is boosted or one of the big projects is killed—the CBO predicts that either Big Science will starve small science, or Congress will underfund the big projects and "nothing will get done" on them, says Webre.

FOR GIBSON AND FISHER
A SEMINAL EVENT IN THE
SHAREHOLDER MOVEMENT



EXECUTIVE SUITE

TIME WARNER FEELS THE FORCE OF SHAREHOLDER POWER

How a wary SEC—and mad-as-hell investors—shot down a ‘coercive’ financing plan

This is to advise you that the Board of Directors of Time Warner Inc. has reviewed its plan to build common equity through its previously announced rights offering in light of comments and objections received from certain stockholders and the Securities & Exchange Commission...[and has] approved certain revisions to the original rights offering proposal.

—July 12 letter to shareholders

With those leaden words, the world's biggest communications company closed an extraordinary chapter in its history. In just over five weeks, Time Warner was forced by a shareholders' revolt and regulatory pressure to turn tail: On July 14, the humbled company replaced its highly unorthodox plan to issue 34.5 million new shares—priced at \$63 to \$105 depending on how many stockholders participated—with an underwritten, \$80-a-share deal. “This could be a seminal event in the shareholder movement,” says David F. Eisner, senior vice-presi-

dent of Providence Capital Inc., an adviser to two angry institutions.

It's hard to think of another recent episode that incited more vehement shareholder opposition—unless it's Time Inc.'s 1989 decision to reject a \$200-a-share bid from Paramount Communications and purchase Warner Communications instead. Still smarting over that, Time Warner shareholders of all stripes—money managers, pension funds, mutual funds, banks, trustees, and individuals—sprang into action, setting off an avalanche of protest.

SLEW OF SUITS. They complained to the company, the SEC, and the press. They asked their investment managers to object. They sued in 14 separate actions. Nineteen members of the Council of Institutional Investors (CII) wrote to Time Warner's investment banks, asking the likes of Merrill Lynch Chairman William A. Schreyer and Salomon Brothers Chairman John H. Gutfreund to explain their participation in the deal. Says CII Executive Director Sarah Teslik: “This is a watershed event, not only because it

was effective but also because more than the usual suspects participated.”

Ultimately, SEC opposition to the pricing mechanism was the deal-killer. Says SEC Chairman Richard Breeden: “Fundamentally, the structure did not comply with the Securities Act of 1933.” Still, there's no question that shareholders made a difference.

Such universal opposition was hardly what Time Warner expected on June 6 when Co-Chief Executive Steven J. Ross announced the rights offering. Immediately, some shareholders voted with their feet: Time Warner stock dropped almost five points in 24 hours.

But not Cliff Hinkle, for one. The executive director of the Florida State Board of Administration, along with two public pension-fund managers in Louisiana, sued to halt the deal. “The structure meant you had to make an investment decision without knowing what price you'd pay,” he says. “We didn't want that precedent to be set.”

Not Dale M. Hanson, for another. The CEO of the California Public Employees

irement System had
n stewing because
hadn't fought Time
en it spurned Para-
ant, a move that cost
PERS more than \$55
lion. In mid-June,
PERS hired Providence
Capital to "see
at could be done."
and not plenty of ma-
money managers,
o blasted the deal
dically and to Time
rner. "No one had
dreamed up a coer-
e equity financing
ore," says Capital
ardian Trust Chair-
n Robert G. Kirby.
e told them we

"I don't like it." That's what Providence
Capital heard when it canvassed holders
more than 40% of Time Warner's
stock. Only one, INB Financial Corp., the
financially for more than 1 million shares,
had CalPERS as a client of the invest-
ment bank. But most seemed to favor
Providence Capital's plan to ask Time
Warner to switch to a fixed-price deal.

FEES. Even so, for a while, Ross, Co-
CEO Nicholas J. Nicholas Jr., and other
Time Warner executives persisted in be-
lieving that shareholders opposed the
deal because they didn't understand it.
Need, the deal was extremely complex.
Explanation didn't help. When Providence
Capital, with CalPERS' O.K., made
presentation to CII's executive commit-
tee on June 27, members "got more up-
as they understood it more," says
attendee. They saw the plan's slid-
ing scale, designed by Merrill Lynch, as
coercive, and they hated the fat fees
brokers would get—up to \$145 million.
As a result, CII decided to pressure
Wall Street with letters to the bankers.
The first letter from the AFL-CIO to Mer-
edith Schreyer: "Your role in promoting
this blind rights offering of this nature is
questionable because many of the hundreds
of Taft-Hartley pension funds we repre-
sent rely on your fiduciary judgment to
invest the retirement savings of millions
of our members and retirees."

By early July, complaints were pour-
ing in to the SEC—including a six-page
letter from Providence Capital that
questioned the legality of the pricing
method and the adequacy of disclosure.
The SEC needed little prompting: Its
staff had raised problems with the pric-
ing mechanism in June. Although the
agency had approved a few similar
plans, the SEC thought Time Warner's
plan violated the 1933 Securities Act be-
cause its price range was so broad,
which effectively kept investors from
knowing the price at which they were
committing to buy. Just as bad, inves-

WHY THE OFFERING RAN INTO TROUBLE

THE LAW

A prospectus must include...the price at which it is proposed that the security shall be offered to the public or the method by which such price is computed and any variation therefrom at which any portion of such security is proposed to be offered to any persons or classes of persons, other than underwriters, naming them or specifying the class. —Securities Act of 1933, Schedule A, Item 16

THE SHAREHOLDERS' CASE

We believe this requirement...is intended to ensure that a purchaser of securities in a public offering knows or has a reasonable basis on which to compute the purchase price.... We further believe that a method of determining price which is unrelated to market price or another objective measure of value, and which is entirely dependent upon facts which are not within anyone's control and results in an extraordinary range of possible prices from \$63 to \$105 per share, does not meet the requirement of Item 16. —Providence Capital's July 3 letter to the SEC

tors were penalized if too many sub-
scribed. "This method was coercive,"
says a senior SEC official.

The SEC had another problem, too—
the same one that troubled many institu-
tions: If Time Warner got the go-ahead,
who else would follow? With troubled
banks and insurance companies looking
everywhere for new capital—not to men-
tion other cash-hungry companies—
would this deal become the financial ve-
hicle of the '90s?

Still, Time Warner wasn't giving up.
In a meeting with staff from the SEC's
legal, market-regulation, and corpora-
tion-finance units, its attorneys tried ev-
ery imaginable argument. They enlisted
support from Louis Loss, a Harvard
University professor emeritus consid-
ered the dean of securities lawyers.
Then, after a long conference call with
Linda C. Quinn, the corporation-finance
division's director, in which she outlined
her objections, Time Warner's legal en-
tourage—including in-house counsel,

outside counsel, and at-
torneys for each of the
eight investment banks
in the deal—decided to
descend on the SEC in
Washington. On July 9,
they met with Breeden,
Quinn, and others.
Breeden objected, too—
but said he wouldn't
make his final decision
until the next day.

When Breeden called
on July 10, the news
was bad: He wouldn't
budge. "[The plan] was
an unprecedented struc-
ture, and it failed to
provide the fundamen-
tal information neces-
sary for shareholders to

make an informed decision," Breeden
says. Still, he made it clear that Time
Warner was welcome to bring the mat-
ter before the full commission.

All along, investor sentiment was con-
verging: If Time Warner needs the mon-
ey—and it does if it's going to make a
\$4.3 billion payment due by March,
1993—it should switch to a smaller,
fixed-price transaction. It was at this
point, say sources close to the company,
that the shareholder dissent was pivotal.
Rather than try to win the debate with
the SEC, further delaying its strategic
plans, Time Warner chose to capitulate.

On Monday, July 8, Time Warner
asked Salomon to design an underwrit-
ten, fixed-price deal. A Salomon team
did, presenting its plan to raise \$2.8 bil-
lion to Ross at his Manhattan apartment
on Wednesday night. When Gutfreund
said Salomon would underwrite up to
half of the deal at \$80 a share—and
asked for a day to seek the rest—Ross
shook hands. The board signed off on
Friday; the SEC followed on Monday.

NEW CONVERTS. Both Time Warner ex-
ecutives and stockholders are bruised. But
many shareholders believe they have
proven a point: When they act cohesively,
they can influence management even
outside the proxy season. In fact, the
experience may have made some new
converts to activism, particularly among
private institutions. Some say they will
reward six-month-old Providence Capital
by giving the broker-dealer trading busi-
ness. Says Providence President Herbert
A. Denton: "That's a tacit admission that
they like what we are all about."

Shareholders wish Time Warner was
converted, too. Says INB Senior Vice-
President P. Roger Kumler: "We hope
this is the first step of management re-
cognizing that the company has to be run
with an eye to shareholder value."

By Judith H. Dobrynski in New York,
with Dean Foust in Washington and
Blanca Riemer in Paris

RUMORS OF A RIFT

Did Time Warner's capital-raising
plans split its top management?
BUSINESS WEEK has learned that
Co-CEO Nick Nicholas opposed the origi-
nal rights issue and favored an offer-
ing akin to the current plan. Co-CEO
Steve Ross, however, strongly argued
for the sliding-scale deal. When the
plan went before the board, Nicholas
backed it. After what director Henry
Luce III calls "surprisingly little discus-
sion," it was approved unanimously.
Nicholas has kept a low profile since
the deal was announced.

But he may not gain for having been
right. Insiders see Nicholas as too
numbers-oriented and believe Vice-
Chairman Gerald M. Levin is now a
Ross ally and a rival to Nicholas. Time
Warner is mum.

PANICKY POLICYHOLDERS HAVE INSURERS TREMBLING

A run by customers forced regulators to seize a shaky Mutual Benefit. It could happen again

In a chilling reprise of the Great Depression, customers have been lining up to withdraw their money. But this time, the lines have been forming outside big and deeply troubled life insurance companies, not banks. Last April, it was Executive Life Insurance Co. In May, it was First Capital Life Insurance Group. For these life insurers, already stumbling under a load of bad assets, the policyholder runs were the final blow, removing whatever chance they had of pulling through. Before the bleeding became fatal and the insurers couldn't meet obligations, state regulators took over.

Now, there is a new casualty—the largest insurance failure ever: Mutual Benefit Life Insurance Co. in Newark, N.J., seized by state regulators on July 16. Over the past three months, as reports of Mutual Benefit's problems accumulated, policyholders withdrew some \$500 million. Mutual Benefit was not yet insolvent, but regulators rushed in to stem the hemorrhaging. "Mutual Benefit could have worked out the problems," says Louise M. Firth, a vice-president at Arthur D. Little Inc. "The run did them in."

NEW TROUBLE. Unlike banks, which had a long history of runs until the advent of the Federal Deposit Insurance Corp. in 1933, life insurers aren't used to such panics. Until recently, insurance collapses were back-page news involving minor-league property/casualty or health insurers. Failed life insurers were quite small. Yet the recent string



CASHING IN: CUSTOMERS HAVE WITHDRAWN \$500 MILLION SINCE APRIL

of mammoth failures, plus widespread reports of the asset woes of such industry leaders as Equitable Life Assurance Society of the U.S. and Travelers Corp., has clearly shaken public confidence. Last winter, Equitable was forced to mount a hard-charging campaign to combat rumors that it was insolvent, which threatened to create a run.

Life insurers are much more vulnerable to runs than banks and thrifts, whose depositors are protected by fed-

eral insurance funds. Policyholders, who depend on life companies for death benefits and retirement income, are quickly learning that their only protection is loophole-ridden state guaranty funds, which are fed by assessments on healthy insurers. Many funds are only large enough to bail out victims of small collapses. According to a U.S. Senate study, the funds of California, Florida, Nevada, and Texas would be depleted if losses at Executive Life exceed \$1.5 billion.

FUNDLESS. Just as bad, the extent of these funds coverage varies wildly by state. Only 20 states, for instance, cover guaranteed-investment contracts or GICs, insurer-run investment vehicles for pension plans. Not until the very eve of Mutual Benefit's takeover did New Jersey even have a fund. Only Louisiana and Washington, D.C., remain fundless.

Heedless of the risks large life companies such as Mutual Benefit in the 1980s set themselves up for a fall. To compete with mutual funds and other new rivals, they shed their conservative investing habits. Executive Life and First Capital have received much attention for their excessive investments in junk bonds. But they were exceptions. Mutual Benefit's choice of a retrorocket, ominously, was more typical of life insurers: real estate.

For a while, the strategy kept Mutual Benefit, founded in 1845, in the game. The 18th-largest life insurer in the U.S., it boasted 400,000 policyhold-

200,000 annuity contracts, and \$13.8 billion in assets. Led by energetic CEO Henry E. Kates, Mutual Benefit leapt with its assets into GICs and other retirement products. In order to deliver fat returns, it sunk billions of dollars in the booming real estate market. The insurer now has 38% of its assets in property or mortgages, higher than the industry average for life companies.



CEO KATES: OUSTED THIS WEEK



NEW CEO STEPHEN CARLOTTI

MONEY. Fisher Island is a good example of the company's vast and misguided ambitions. The half-finished \$25 billion luxury condominium development, located off the southern tip of Miami Beach, is meant for the big-money crowd. Units are priced as high as \$1 million. This Shangri-la has two pools that can accommodate 200-foot yachts, seven gourmet restaurants, a spa, and sand imported from the Bahamas. All this cost Mutual Benefit a fortune, and expensive construction mistakes didn't help. According to consultant Michael Y. Cannon, who used to work for Fisher Island, roads had to be torn up because they didn't meet the building code.

All that would be acceptable if sales were brisk. But since mid-1990, they have been dead, and the place is a big drain on the company. "Things got slow when the recession started and it slowed during the war," admits Stephen J. Carlotti, who is replacing Kates as CEO at the state's behest. Carlotti claims sales at Fisher have started to rebound and predicts a turnaround in two to three years.

When the real estate market tanked, Mutual Benefit went down. Nearly 10% of its mortgages were in default by the end of 1990, almost triple the average level for life companies. It began to foreclose aggressively on bad loans, but that left an inventory of sorry properties. One was Boston's landmark Park Square building, where the vacancy rate is 45%, up from 25% in December. Mutual Benefit's cushion shrank an alarming 7% in 1991's

first quarter alone (chart). The insurer tried to raise cash by selling part of its operations to Metropolitan Life Insurance Co., but that flopped. Next, Mutual Benefit asked Smith Barney, Harris Upham & Co. to recruit another investor. None emerged. It announced a 20% layoff of its 3,100 staff. The credit ratings agencies weren't impressed. In May, Standard & Poor's Corp. downgraded Mutual Benefit's claims-paying ability by four notches, from second-ranked AA+ to A.

'SELF-FULFILLING PROPHECY.' The downgrades touched off the run. "Coming on the heels of Executive Life and First Capital, people got very nervous," says new CEO Carlotti. "They wouldn't listen to us. They wanted their money back, and this became a self-fulfilling prophecy." Another piece of bad news came July 8 when A. M. Best Co., the venerable insurance rating service sometimes criticized as too easy on companies, belatedly lowered Mutual Benefit from its highest to its second-highest grade. As the policy surrenders grew to a torrent, regulators opened

quiet discussions about a take-over. After a published report of these talks on July 12, policyholders jammed the company's lobby to make redemption requests. "We concluded," says Carlotti, "that this simply wasn't going to end."

New Jersey's action stabilizes Mutual Benefit's finances for now. Policy surrenders and loans are forbidden. Only death benefits and policy cash-outs in hardship cases are O.K. At least Mutual Benefit annuity recipients won't suffer a cut in payments, which leaves them much better off than those of Executive Life's California subsidiary, whose benefits were slashed by 30%. As is the case with Executive Life, regulators hope to sell off Mutual Benefit, or at least its robust group health unit. A four-star name—Nicholas D. Katzenbach, Attorney General under President Johnson—was imported to oversee the company for the state, supervising Carlotti. In a bid to attract fresh business, the state also lined up two of the largest insurers, Prudential Insurance Co. of America and Met Life, to stand behind any new policies written.

So what big insurer will be next to be hit with a run? While the shape of the industry is sound overall, several major players seem vulnerable. "After Executive Life, I predicted there would be no more," says Daniel R. Gattis, senior vice-president with consultant SEI Corp. "Well, I could be wrong again." Given the panic factor, that's a decent bet.

By Larry Light in New York, with Julie Lopez in Trenton, N. J., and Antonio N. Fins in Miami



TROUBLE AT MUTUAL'S \$1.25 BILLION FISHER ISLAND CONDO ADDED TO ITS WOES



GOOD TIMES: JOSEPH FESHBACH, KURT FESHBACH, AND PARTNER TOM BARTON IN 1990

THESE SHORTS AREN'T LAUGHING NOW

Rising stocks are pummeling short-sellers such as the Feshbachs

Joseph Feshbach, short-seller extraordinaire, is unbowed—but bloodied. In just the past seven months, as the Dow Jones industrial average has flirted with 3000, the \$1 billion partnership run by Feshbach and his brothers has dwindled to \$500 million. The brothers have even put up for sale their Challenger 601 jet, which they bought for \$10.8 million only last year. Still, the Palo Alto (Calif.) brothers are hanging tough. Says Joe: “The market hasn’t changed so significantly that we don’t have a chance of getting back on a winning path.”

For the scores of short-selling partnerships scattered throughout the country—and their uncounted thousands of investors—the market’s recent vibrancy has meant only heartache.

Shorts bet on stock-price declines by selling borrowed shares, hoping to buy them back at a lower price. It’s a strategy that works well when stocks are in the doldrums—as they were through most of 1990. But it was a dramatically different story beginning in the fourth quarter of 1990 and continuing in the wartime rebound in January, when the market surged—in a rally led by short-selling favorites, ranging from high-technology stocks to money-center

banks (table). And although the market has treaded water since then, short portfolios are believed to have recovered by an average of only about 3% to 4%. “Since the fourth quarter of last year, it’s been awful,” laments Neil Dolinsky, vice-president of C. C. Dunnavan & Co., a Minneapolis money manager that dabbles in short-selling. “The worst stocks are the ones that go up most.” Dolinsky’s \$27 million in short positions has shrunk to \$2 million, after a foundation surveyed the wreckage and yanked out its money in June.

As a result, short-only partnerships have fallen into a crater. And they’ll be there for a while, because most are structured so that they must recoup any losses before the general partners can draw a penny in performance fees. “This year, most short-sellers will count themselves lucky if they break even. We’ll be very happy if we make everybody whole,” says Michael Kaatz, a prominent

‘It’s been awful.
The worst stocks are the ones
that go up the most’

short-seller and senior partner of Renard Asset Management.

What went wrong? Some short-seller and market observers maintain that widely shorted stocks were deliberately targeted by speculators—in an effort to force short-sellers to replace their borrowed shares, thereby driving up share prices. “There has been a lot of short bashing,” asserts Bruce Hauptmann, a Iowa-based consultant who tracks private investment partnerships. The culprits: mutual funds and even some hedge funds, which often go short themselves. “It was the first time shorts were targeted en masse,” says Michael Murphy, editor of *Overpriced Stock Service*, a newsletter catering to short-sellers.

An even more crucial negative is that short-selling has become too popular. When stocks tanked in 1990 and short portfolios commonly gained 50%, institutions poured money into short portfolios. The Feshbachs’ assets under management rose from less than \$1 million in the early 1980s to an unwieldy \$1 billion in late 1990. So the big short-sellers have shifted from their traditional forte—small, overheated stocks—toward bets on broad economic trends by investments in large-capitalization stocks. “As more and more money comes in, you have to change the way you do business,” notes Clifford W. Henry, general partner of Worthington Growth LP, a hedge fund that does considerable short-selling. “Small stocks have very little impact on your portfolio. But you can short big stocks easily if you’re a large short-seller, because there’s a lot of shares available to borrow.”

JUNK RISES. Bank stocks have long been at the top of the short-seller hit list because of their much chronicled troubles in real estate lending—but most shorts were surprised by the first-quarter rally in financial institutions. Among the short favorites were Manufacturers Hanover Corp., whose shares gained handsomely in recent days because of its upcoming merger with Chemical Banking Corp.

Likewise, shorts have targeted companies with large debt levels, such as Marriott Corp., the hotel chain, and Household International Inc., only to see their shares rally nevertheless. “We’re skeptical how real the recovery is. If there’s a recovery, it will be fairly anemic,” says Kaatz, whose \$16.5 million short-selling fund gained 70% in 1990, only to fall 20% in the year to date. Kaatz argues that the first-quarter slaughter was an anomaly because junky stocks rose more than good stocks. “When the tide rises strongly, leaky boats go up, too,” says Kaatz. And this time around, he main-

Success comes in many varieties.

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with their myriad colors and shapes, butterflies are among nature's most richly varied species. Rich variety is also found in the colors, shapes and patterns of "Ceran" cooktop panels. A rangetop that's proved so successful that over 12 million have been sold worldwide since 1972.

It's hard to beat butterflies when it comes to the variety of colors and shapes. In fact, some 150,000 distinct butterfly species are found throughout the world.

While not quite as diverse as the butterfly, variety is also a key to the success of "Ceran" glass-ceramic cooktop panels.

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To die-hard shorts, the market is still temptingly overvalued. The Standard & Poor's 400-industrial-stock index, bears say, is now more than 3.2 times book value and nearly 20 times earnings. Those multiples, Kaatz maintains, are higher than just before the market crashes of 1929 and 1929.

Still, Kaatz and other short-sellers are trading more conservatively. They are using less leverage and are quicker to cover short positions when the market moves against them—instead of stubbornly holding on to a short position, hoping for a decline.

NAKED CALLS. Riskier strategies, too, are falling out of favor. One is an options-trading strategy used by some shorts, involving selling options that give the buyer the right to buy stocks at a certain price. That's known as "writing a call option," and when the person selling the option does not own the stock, the call is "naked"—and it can be mighty perilous. One short-seller that is an active writer of naked calls is Chicago-based Gilford Partners, a venerable short-selling partnership that is among the firms believed to have sustained large losses in the past year. Gilford's general partner, Robert Holmes, maintains that the partnership remains "profitable," but he declines to disclose performance figures.

SHORT FAVORITES HAVE BACKFIRED THIS YEAR

Stocks with the largest short positions on Jan. 15

	Number of shares Millions	Share price 1/15/91	Share price 7/17/91	Percent change
CITICORP	16.9	12 1/4	14 3/8	17.3%
GTE	14.8	28 1/4	29 3/8	4.0
ELI LILLY	14.1	69 1/2	73 3/8	5.6
VARIETY	12.4	1 3/4	2 3/8	35.7
MARRIOTT	10.9	9 3/4	17 3/4	82.1
CHRYSLER	10.8	12 5/8	14	10.9
FED. NATL. MORTG.	10.7	34	53 7/8	58.5
BANK OF BOSTON	7.9	4 1/2	8 1/4	83.3
CHEMICAL WASTE	7.2	21 3/8	18	-15.8
HOME DEPOT	7.1	25 1/4	47 5/8	88.6
NEWS CORP. ADRs	6.6	6 1/4	12 1/2	100.0
BLACK & DECKER	6.5	8 3/4	16 3/8	87.1
PAN AM	6.4	11 1/16	11 3/32	-50.0
CONTINENTAL AIR	6.4	1 5/8	1 7/8	15.4
FRUIT OF THE LOOM	6.1	8 1/8	15	84.6
BALLY	6.0	2	3 7/8	93.8
L.A. GEAR	5.8	12 1/4	12	-2.0
WELLS FARGO	5.4	49 3/4	71 1/8	43.0

DATA: BW

Despite their recent woes, short-sellers still enjoy a major advantage over "longs": a nearly unbreachable veil of secrecy. Shorts raise money almost exclusively through private partnerships, which are not required to disclose their holdings, strategies, or performance. And shorts have no obligation to disclose even if they are short a substantial por-

tion of a company's stock. The Securities & Exchange Commission is circulating for public comment a proposal requiring short-sellers to disclose short-selling of more than 5% of a company's shares. But SEC officials are skeptical, and the plan stands little chance of adoption.

Without a major regulatory roadblock, the biggest shorts of all, the Feshbachs, can continue their stock-busting pursuits. Joe Feshbach says the brothers are still short a number of banks, insurance companies, leasing firms, and other financial institutions—the same kinds of stocks they've shorted over the past five or six years. They still "have a meaningful interest" in Wells Fargo & Co. "We continue to think its asset quality is highly suspect," he says.

Other Feshbach picks include Citicorp—which, he notes, has failed to earn its dividend in the last three quarters but continues to pay it. The brothers also are short insurance holding companies Conseco Inc. ("no tangible common equity") and NWN Cos. ("exposure to high-risk real estate"). Insurance companies are the "next wave of disaster," Feshbach says. "We're used to watching apparently Teale-coated institutions skate by for a few quarters," he says, "and then wake up to bigger problems." Investors in short-selling ventures know that all too well.

By Maria Shao in San Francisco and Gary Weiss in New York, with bureau reports

SCAMS

FAILED INSURERS: A COMMON THREAD?

A consultant is allegedly tied to collapsed companies

In November, 1988, Georgia insurance regulators shut down Victoria Insurance Co., a small insurer that, among other things, wrote policies for professional athletes. In April, 1990, International Forum of Florida (IFF), a health-insurance marketer, was placed in receivership. On June 6 of this year, Pennsylvania insurance officials suspended World Life & Health Insurance Co., which wrote accident and health policies.

At first glance the failures appear unrelated. Yet investigators for the Senate permanent subcommittee on investigations have uncovered some curious connections. Unlike the seizure of Mutual

Benefit Life Insurance Co., the collapse of these three small companies involved allegations of financial finagling. IFF's demise, says Bernard H. Dempsey Jr., an Orlando lawyer who represents the state, was "a massive conspiracy and fraud on the people of the state of Florida."

All three had substantial dealings with Alan Teale, a British-born insurance consultant. From his office in Atlanta,

Teale controls a network, say Senate investigators, of at least 19 insurers and reinsurers, many of them offshore and unregulated. While associates have testified that Teale maintains an arm's-length relationship with the companies,

a report by the subcommittee concludes: "When the layers are peeled back, we found that Alan Teale is at the controls."

Teale, who has not been charged with any crime, is scheduled to testify on July 19 before the subcommittee, which is conducting a wide-ranging probe of insurance fraud. In a brief conversation with BUSINESS WEEK, Teale declined to answer questions about his activities. Senate investigators and state regulators believe Teale typifies a growing group of individuals who operate on the fringes of the in-



TEALE: "AT THE CONTROLS"

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the industry and particularly of the \$23 billion reinsurance business. Reinsurers take on risk from insurers who want to reduce their exposure. Teale and others, say officials, exploit the loose network of state insurance regulation and the absence of federal regulation. Documents assembled by investigators suggest that Teale starts new insurance companies or offers help to existing insurers that have fallen on bad times. Then, say investigators, companies with ties to Teale find ways to siphon off the insurers' assets. "The same people keep showing up again and again," says Delaware Insurance Commissioner David Levinson. "That's why we need a federal antifraud statute."

Lawmakers are examining Teale's role in recent insolvencies. Attorneys for the three companies linked to him could not be reached for comment.

NO RENEWAL. Teale trades on his background as a former official of the British Insurance Brokers Assn. and his contacts with the venerable Lloyd's of London. His glowing résumé was what attracted officials of the Miami-based Insurance Exchange of the Americas to him. In 1981, he was hired to head the Lloyd's-style market, which specialized in hard-to-insure risks. Exchange officials declined to renew Teale's contract in 1984, however, because he lacked management experience. Three years later, the exchange was placed in rehabilitation, leaving \$200 million in outstanding claims. Lawsuits against the exchange have alleged fraud, including wide dealings with offshore reinsurers. Teale hasn't been implicated in the exchange's demise.

Among Teale's first ventures was Victoria Insurance, which he started in April, 1987. Victoria began with \$1.2 million in capital, but within weeks of its inception, Georgia officials later learned, the company transferred \$1.2 million from its Atlanta bank to an account in London. Victoria was apparently insolvent almost from the start.

Nevertheless, Victoria wrote \$16 million of business in just 18 months. One of Victoria's prime markets was insuring athletes against career-ending injuries. Among those who signed up were Los Angeles Raiders running back Bo Jackson, former Philadelphia Eagles cornerback Roynell Young, Buffalo Bills quarterback Jim Kelly, and Atlanta Fal-



ATHLETES YOUNG, KELLY, AND FLOWERS AT VICTORIA INSURANCE HEARINGS

cons ex-running back Kenny Flowers.

Georgia investigators found that more than \$10 million in Victoria premiums had been siphoned into Swiss bank accounts. And some \$20 million in assets apparently were deposited in Paris with a firm called Goldman Dollar Securities. But Georgia regulators found no such outfit existed. Today, says the Georgia Insurance Dept., Victoria has \$20 million in unpaid claims but less than \$700,000 in assets.

IFF was Teale's next prospect. The company was facing pressure from state officials to shore up its finances. In September, 1989, Teale's firm offered to help the company boost its assets through an infusion of mortgage-backed securities. The Florida regulators believe Teale and his associates never owned the securities and that the transaction was just a sham. The regulators claim it was designed to keep IFF in business by

artificially boosting its capital.

While IFF continued to operate, entities associated with Teale allegedly profited from its dealings with reinsurers. The reinsurers were recruited by the World Re brokerage, one of whose directors is Charlotte Rentz, Teale's wife, who could not be reached for comment. World Re earns fees for its work, and the reinsurers profit as well. The reinsurers

later refused to honor IFF's claims, alleging that it had engaged in securities fraud. When IFF collapsed in 1990, it left 8,000 policyholders and \$16 million in unpaid claims. A federal grand jury in Orlando is examining the debacle. In a lawsuit against Teale, IFF, and others, Florida regulators have accused Teale of such misdeeds as "theft."

WISE OTTER. Another company to accept Teale's offers of help was financially troubled World Life in King of Prussia, Pa. In 1989, World Re offered to handle World Life's reinsurance. As the broker, World Re controlled what was supposed to have been a \$6.2 million escrow account holding money for payment of World Life claims. But investigator found that the account was short by about \$4.7 million, partly because it counted as assets a portfolio of nearly worthless penny stocks.

Investigators also discovered that the reinsurers World Re signed up were weak financially. One listed as its primary assets \$22 million in alleged "treasury bills" issued by a Texas Indian tribe that Senate investigators believe is fictitious. One of the tribe's alleged leaders, who calls himself Wise Otter, is a British business associate of Teale's. He could not be reached for comment.

The Senate probe doesn't seem to have slowed Teale down. In California, U.S. & Continental Reinsurance Co., a Belgium-based reinsurance company founded by Teale, has written \$50 million in auto insurance, say state regulators. On July 10, regulators advised California brokers not to do business with U.S. & Continental, which also happened to be one of World Life's reinsurers.

Regulators may be catching on to Teale's modus operandi. But with insurance insolvencies growing, stories such as Teale's will only increase the clamor for federal regulation.

By Tim Smart in Washington, with Gail De George in Miami

ALAN TEALE'S CIRCUITOUS CAREER

1981-84

Teale heads the Miami-based Insurance Exchange of the Americas. Three years later, it collapses

1987-88

He launches Victoria Insurance. It is shut down by Georgia insurance officials in 1988 amid fraud allegations

1989

Teale gets involved with International Forum of Florida, a health insurance firm. It collapses in April, 1990. State officials sue Teale and others for fraud

1990-91

Teale assists Pennsylvania-based World Life & Health Insurance Co. in bolstering its finances. Investigators uncover financial irregularities. State regulators suspend operations in June, 1991

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UNIFI IS SPINNING A POLYESTER POWERHOUSE

Since the October stock market bottom, Unifi has nearly tripled, to 37. No, Unifi isn't a hot biotechnology company—it's a major player in polyester.

Don't snicker. Unifi is no joke. The Greensboro (N. C.) company "texturizes" raw polyester fibers—an intermediate step between manufacturing the synthetic material and weaving it into fabric. Unifi is starting to produce the raw fibers, too. It already does so at a plant in Ireland, and it plans to build a facility in North Carolina.

Unifi could benefit from the growing popularity of "microfibers"—new forms of polyester that look and feel like natural fibers. Big-name designers such as Mary McFadden and Donna Karan are introducing microfibers into their clothing lines. Company officials note that microfibers are still too costly for the mass market. No matter: Unifi thrives on plain polyester. Earnings have grown at a compounded annual rate of 17% since 1981—even though polyester peaked, along with leisure suits, back in the '70s.

There's more good news: On Aug. 7, the company plans to merge with Macfield, a privately held yarn processor with \$489 million in sales, in a stock swap valued at \$350 million. The combined company will have about \$1 billion in sales and a stock market capitalization of more than \$1 billion, which will make it the nation's largest publicly held textile company.

That heft should attract more followers on Wall Street and introduce the company to investors who would have dismissed it as too small before. Says money manager William Martindale of Martindale, Andres & Godshalk: "Unifi is an investment-grade vehicle of the future."

'TREMENDOUSLY EFFICIENT.' Unifi earns a return on equity of better than 20%—and does it with a debt-free balance sheet. "Management spends heavily on equipment, and they're tremendously efficient throughout the operation," says William D. Witter, a money manager at the firm that bears his name.

Management is deft on finances, too. In recent years, Unifi repurchased 3.6 million shares at an average price of \$15.64. Then, on June 28, it sold 3 mil-



lion shares at \$33.25 each. The proceeds will pay off Macfield's debt.

Analysts expect Unifi to earn \$1.94 a share for the fiscal year that ended June 30. Martindale thinks earnings will be in the \$2.50-to-\$3 range for fiscal 1992. In addition, he says the company's commitment to pay out 30% of aftertax earnings means the annual dividend could rise from 40¢ in fiscal 1991 to 90¢ in 1992. All told, he expects the stock to be north of 50 next year.

TREMONT'S CLASSY NEW LOOK

Nobody paid attention to Tremont when it debuted on the Big Board last October. That's because the titanium producer had just been spun off from Baroid and traded at \$1 to \$2 a share. That made it a penny stock, which, in the bear market, had all the allure of a toxic-waste dump. Never mind that Tremont was light on debt and rolling in cash.

But now, the company is bidding for respectability. In May, shareholders enacted a reverse split, getting 1 share for every 10 they owned. Then, the directors instituted a 20¢ quarterly dividend. Now, Tremont is a \$20-a-share stock with a plump 4% yield. There's also \$18 a share in cash and \$31 in book value.

What's holding Tremont back is the presence of takeover artist Harold Simmons. Simmons' Valhi owns major pieces of Tremont and Baroid and is the majority shareholder of NL Industries—which spun off Baroid in 1988. "People think Simmons will use Tremont's cash for his next raid," says

Hugh Denison, research director at Heartland Funds.

That's a switch. Back in the '80s, Simmons' raids made millions, and investors wanted in on his deals. But he lost his last fight (for Lockheed), and raiders are out of favor.

Shareholders Denison and Nikos Monoyios of Guardian Investor Service won't mind if Simmons uses Tremont for a raid, but that's not why they bought the stock. "It's a good long-term value, with an excellent balance sheet and a leading position in its industry," says Monoyios. Titanium, a strong but light metal, is used primarily in aircraft. "I wouldn't be surprised if the company earned \$2 a share this year," says Denison. "And if the sun shines, it could earn \$4."

SIFTING THROUGH EASTERN'S RUBBLE

In its last years, Eastern Air Lines lost millions. But now that Eastern is in liquidation, Charles Lemonides, who analyzes distressed securities for Gruntal, thinks there are some profits to be had in the dead airline.

Lemonides likes Eastern's 2nd Priority Secured Equipment Certificates, which trade on the American Stock Exchange. He says the certificates are a steal at the recent price of 65. That's \$650 for a certificate with a \$1,000 face value. Lemonides thinks investors should realize a return on investment anywhere from 57% to 112%. The payoff could come in 10 to 26 months, he says, depending on how fast the trustee can sell the planes that are the security for the certificates.

There's \$168 million in certificates at par, but that's only \$109 million at today's market price. What's backing them now is \$50 million in cash and 58 aircraft, which suggests a value of less than \$1 million per plane. Even though the used-aircraft market is hardly robust, Lemonides argues that the price is too low. "The engines alone are worth \$500,000 each," he says.

Consultants asked by the analyst to value the planes came up with \$263 million. To be conservative, Lemonides figures the planes would fetch half that. He also allows \$20 million for maintenance. That leaves \$111 million. Add the cash plus interest earned on the cash, and he comes up with \$169 million, or \$1,020 for a certificate selling for \$650. If the planes sell for 75% of their estimated value, the certificates could be redeemed at \$1,380.

CREDIT BUREAUS: CONSUMERS ARE STEWING—AND SUING

They're livid over error-ridden reports that deem them bad risks

It's been building for years. Consumers have been complaining that companies that collect and sell credit data have often been careless, callous, and uncooperative when it comes to cleaning up errors in their electronic files. A bad report can keep a consumer from getting a mortgage, a car loan, or sometimes even a job. And, consumers have once erroneous information such as a false record of a missed loan payment slip its way into the data banks, it can be a hassle to erase it.

Now, the complaints have grown so loud that politicians are smelling votes. On July 9, six states brought two suits against Cleveland-based TRW Inc., which is one of the three largest credit bureaus. The first, brought by Texas and led by California, Alabama, Idaho, and Michigan, alleges that TRW fails to ensure the accuracy of its data and doesn't correct mistakes quickly enough. It also contends that TRW violates con-

sumers' privacy by selling financial data about them to direct marketers.

A second suit in New York makes similar allegations. Both charge that TRW acts not as a mere repository of credit data on 170 million Americans but "secretly" rates them for "creditworthiness" and doesn't show them the ratings. TRW, which says the law doesn't require it to disclose credit scores to consumers, filed a motion for a declaratory judgment to nullify both suits.

BIG RESPONSE. But the TRW litigation is already drawing a big response from the public, says New York State Attorney General Robert Abrams, who is seeking the Democratic nomination to challenge Senator Alphonse M. D'Amato in 1992. "I can't remember a case that has caused so many people to stop and talk to me," he says. "It cuts a wide swath across the population."

Before more politicians pile on, some players in the \$1 billion U.S. credit re-

porting industry are trying to head off a consumer backlash. On July 15, Atlanta-based Equifax Inc., another top credit bureau, announced plans to set up a toll-free customer service center staffed by more than 500 consultants who can resolve disputes quickly. The move will be costly: Equifax has already taken a \$9 million charge against its first-quarter earnings to pay for the program. On the same day, TRW announced a less ambitious plan to set up an 800 number for consumers who have been denied credit. TRW says it already employs more than 500 service reps, up 50% from last year.

What's more, says John McGee, vice-president for marketing and business affairs at TRW Information Services, TRW adheres to every relevant fair-credit law. McGee says company officials spent hundreds of hours negotiating with law-enforcement officials, mostly in Texas, to head off the suits. "We responded, addressing each issue," he says. McGee adds that the Texas Attorney General's office has been unable to tell him specifically how TRW breaks the law: "Either they can't or they won't."

Whether the charges hold up in court, the suits have tapped a deep vein of consumer frustration. In Texas, Assistant Attorney General Stephen Gardner says his office has received more than 720 complaints about TRW since 1989. That's more than for any other ongoing business. "These are from people who

have tried to solve problems with TRW not just one time, but a number of times," he says.

NAME GAME. Most complaints stem from TRW's alleged failure to fix damaging errors. Paul K. Jacques, a Wyoming resident, was unable to buy a car because negative information about his father, Paul J. Jacques, was in his credit report. When TRW failed to rectify the report over several years, Jacques charged gross negligence and won \$290,000 in damages. TRW is appealing.

TRW concedes that it's difficult for its computers to distinguish between people of similar names and says it is working on new software to address that. The worst case, says McGee, is when two people at the same ad-



ABRAMS: NEW YORK'S SUIT AGAINST TRW IS IMMENSELY POPULAR

WHAT'S FAIR IN CREDIT REPORTING?

Consumer groups are advocating the following:

IMPROVE ACCURACY

Credit bureaus should take responsibility for correcting mistakes no matter where the data came from and should inform other credit reporters of errors

GRANT FREE REPORTS

Consumers should be entitled to a free copy of their credit report once a year, not just when they are denied credit

PROTECT PRIVACY

Consumers should be given a clear chance to prevent sales of personal data to marketers

IMPROVE SERVICE

Credit-denial notices should include a list of consumers' rights. Investigations of errors should take 30 days, tops

BETTER ENFORCEMENT

The Federal Trade Commission should be given more power to penalize credit reporters for violating the law

DATA: U.S. PUBLIC INTEREST RESEARCH GROUP

dress have essentially the same name. "People can name their children whatever they want to, but they just need to understand [the consequences] of doing so," he says.

Many errors begin with simple mistakes. Take the case of Robert Tatum, a part-time college student in Dallas. Tatum's bank incorrectly reported that he was behind on his student loan. The bank had lost his application for deferred payments and quickly fixed the error. But it took TRW six months to update its records. In the meantime, Tatum says, he lost his full-time job because he couldn't get credit to buy a car to get to work. All along, TRW was unresponsive, says Tatum, who says he may sue. TRW says it can't comment on every complaint.

SELF-POLICING? The credit bureau issue has hit Washington, where consumer groups are pushing for more regulation (table, page 69). In response, the House Subcommittee on Consumer Affairs plans to introduce in September legislation to strengthen and update the Fair Credit Reporting Act of 1970.

On the other side is Associated Credit Bureaus, a Washington-based trade group that represents TRW, Equifax, Trans Union, and hundreds of smaller credit agencies. It argues that the industry should be left to police itself. "Anecdotal stories are being used as the basis for sweeping changes," says D. Barry Connelly, executive vice-president of the group. The industry says that the proposed reforms will increase their cost of doing business and bog down a system that helps U.S. consumers buy 5,000 homes, 40,000 cars, and 300,000 major appliances every day. "We're trying to strike the balance between consumer protection and the costs to the industry," says a congressional staffer who works for subcommittee Chairman Esteban E. Torres (D-Calif.).

But the controversy isn't likely to die down quickly. Consumers Union recently scoured 161 credit reports and found that 19% had errors serious enough to cause information buyers to deny credit, employment, or insurance. In June, the Federal Trade Commission said that credit reports are now its biggest source of consumer inquiries and complaints. And American Telephone & Telegraph Co.'s Universal Card unit recently became the first big credit grantor to urge the industry publicly to give consumers better service. With pressure like that, no wonder credit bureaus are trying to cool things down.

By Evan I. Schwartz in New York, with Zachary Schiller in Cleveland, Walecia Konrad in Atlanta, and Stephanie Anderson Forest in Dallas

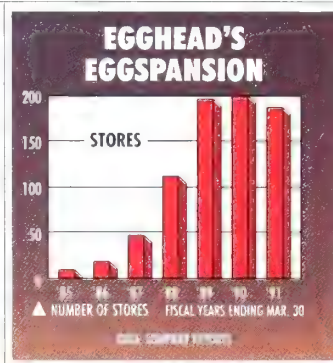
EGGHEAD SCRAMBLES BACK

But now, it faces a price onslaught from computer superstores

All the king's horses and all the king's men couldn't do it for Humpty-Dumpty. But two Seattle executives, Stuart M. Sloan and Matthew J. Griffin, have done it for Professor Egghead, the symbol of the nation's largest software retailer, Egghead Inc. After a great fall—two years of losses and the closing of 29 stores—they have put the seven-year-old company together again.

Sloan, a retail executive, and Griffin, a real estate whiz, took over Egghead two years ago. The deal: They would each get \$1 a year—plus stock options that will pay the pair as much as \$18 million if Egghead's stock hits 20. It now trades at 14, up from 10 when they started.

'WRONG FORMAT.' Under founder and former Chairman Victor D. Alhadeff, Egghead had grown rapidly, nearly doubling the number of stores and adding 1,600 employees in fiscal 1989 alone. But the inventory system was a mess, theft



was rampant, and losses were mounting. Hire by Alhadeff, Sloan and Griffin set up internal controls that encouraged store managers to shape up. It worked. For the year ended May 30, Egghead turned a profit of \$15.4 million on sales of \$519 million, up 14% from fiscal 1990.

But just as Egghead is ready to start expanding again, the 187-store chain faces a new breed of rival: computer superstores.

These warehouse-like outlets, led by the 20-store, \$600 million Comp USA chain, sell computers and software at rock-bottom prices. Within the next 18 months, the number of superstores in the U.S. is expected to more than triple to 144. And within three years, predicts industry consultant Seymour Merrin, these no-frills warehouses will wipe out Egghead Discount Software outlets. Egghead has "the wrong format for this day and age," Merrin says.

Griffin, who took over the CEO slot

Selling service:
CEO Griffin is spending \$3 million this year to make sure salespeople know their stuff



Datacomm Commentary

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—Information Systems Group,
Wendy's International



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from Chairman Sloan in April, laughs when he hears predictions of Egghead's demise. Egghead stores usually suffer during the first year after superstores move into their markets, he says, but they bounce back in the second. Even Nathan Morton, CEO of Dallas-based Comp USA, concedes that Egghead appeals to consumers who may not want to travel extra miles to a suburban superstore. "Our strength is price," he says. "Egghead's is convenience."

To defend against the superstore price competition, Griffin pushes Egghead's advantages in service. He's spending \$3 million to train sales "eggsperts" to give knowledgeable advice to both novices and experienced computer owners. And he has increased the average store selection from 1,300 to 1,600 items.

UNLIKELY PAIR. Another Egghead advantage is a knack for promotions. To draw crowds to its stores, Egghead aggressively promoted Microsoft Corp.'s new MS-DOS 5 operating system with a price of \$39.99, well below the \$99.95 list. "Their merchandising is brilliant," says Scott D. Oki, Microsoft's senior vice-president for sales and marketing.

Sloan and Griffin were an unlikely pair to turn around a high-tech retailer. Sloan, 47, had earned kudos on Wall Street with his 1986 leveraged buyout of grocery chain Quality Food Centers Inc. And Griffin, 39, had made so much money in 11 years at a big real estate company that he still has not cashed in any of his options on Egghead stock.

The pair focused on the company's main businesses: the stores themselves and selling software directly to big businesses, which accounts for 60% of revenue. They divested Egghead's software training program and support service. They also gave store managers profit-and-loss responsibility. Now, they're ready to expand with as many as 30 new stores. But Griffin says he also plans to close 10 stores in poor locations.

Short sellers, who own about 3% of Egghead stock, are betting that the expansion will fail. Sloan and Griffin disagree, but they might not be around to see their plans through. Sloan has already pulled out of day-to-day management. And Griffin, an avid cyclist who once took a year-long bike tour with his wife, says he will find a new CEO after his contract expires in 1993. Hanging on his office wall is a world map with pushpins tracing his 1987 bike trip through Europe, Asia, Australia, and New Zealand. Meanwhile, Latin America—with no pushpins—beckons. But Sloan's unexercised options should keep him interested in making sure that Egghead doesn't crack open again.

By Dori Jones Yang in Seattle, with Stephanie Anderson Forest in Dallas and bureau reports

Economics

CAPITAL

THE U.S. HAS A NEW WEAPON: LOW-COST CAPITAL

That competitive edge could boost growth for years to come

It got no attention at the meeting of the leaders of the major economic powers in London. But the U.S. has scored a victory in its battle to become more competitive in the global economy. In a stunning reversal from the past decade, when America's industrial might was dragged down by a persistently high cost of capital, U.S. companies no longer have to pay more for money than their foreign rivals. And cheaper capital could bolster growth in the U.S. for years to come.

Lower U.S. financing costs mean that companies can afford to invest more in plant and equipment and wait longer for a payback from capital projects. "The cost of capital affects the rate of investment, especially in research and development—the things that could lead the U.S. to be competitive in the future," says George N. Hatsopoulos, chief executive of Thermo Electron Corp., a technology conglomerate based in Waltham, Mass. Adds Robert M. Giordano, an economist at Goldman, Sachs & Co.: "A

raise capital, and here the U.S. is also scoring points. Standard & Poor's 500 stock index is up 9% since the beginning of 1990, while the Nikkei is down by some 40%. The result has been to reduce the huge price-earnings ratio in Japan from a peak of about 67 in December, 1989, to a current level of 43. P-e's in the U.S. have actually risen to 18, from 14. So when a Japanese company now sells shares to raise capital, it is giving up more in the way of earnings for each yen raised than it did two years ago. For a U.S. company the opposite is the case. No wonder the initial public offering market in the U.S. is booming, while the Japanese one is in the doldrums.

Of course, to get an accurate reading of international differences in capital involves a lot more than just totting up the cost of debt and equity. Economists typically adjust their calculations for varying accounting conventions and depreciation rules, inflation rates, and taxes. Capital costs in the second half of the 1980s averaged 7.5% in the U.S., compared with 5.4% in Japan and 4.3% in Germany, according to one such complex calculation by Steven H. Nagourney, chief global strategist at Shearson Lehman Brothers Inc. But by the first half of 1991, capital costs in the U.S. had fallen to 5.9% and risen to 6.1% in Japan and 4.8% in Germany. Says John A. Young, chief executive officer of Hewlett-Packard Co.: "Much of the cost-of-capital advantage of Japan and Germany has gone away."

COST VS. CULTURE. Japan emerged as the world's most feared global competitor in the 1980s. Management savvy played a big role, but a low cost of capital was also an important element. Estimates of financing costs in Japan and the U.S. vary widely, but most studies agree with Nagourney that capital was a lot cheaper in Japan for much of the 1980s. For example, by his calculation, the cost of capital (after adjustments) in the U.S. in 1985 was 9.7% annually, compared with 5.9% in Japan.

This gap strongly affects investment decisions, especially for long-term projects. The 3.8 percentage point difference

Lower inflation, the recovery, and a better profit outlook have fueled a bull market in stocks, lowering money costs

low cost of capital can encourage more risk-taking and more innovation, and maybe more productivity growth."

There is no doubt that capital is getting cheaper in the U.S. and more expensive abroad. In the U.S., short-term rates have fallen by about two percentage points over the past year. One-year U.S. Treasury bills now yield 6.2%, while comparable German debt pays a hefty 8.6%. In Japan, banks are offering 7.6% on three-month certificates of deposit vs. about 5.7% in the U.S. Long-term rates in the U.S. have fallen half a percentage point since May, 1990, while they have risen by half that amount in both Germany and Japan.

Equity financing is another way to

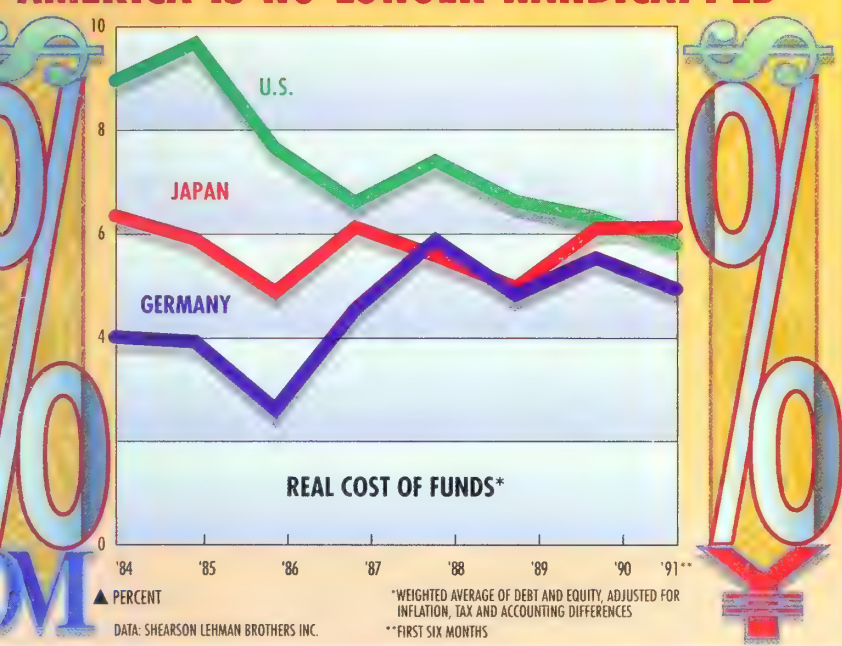
ns that if a U.S. and a Japanese
pany were both considering an in-
ment that would begin to pay off
r five years, the cost of financing
project would be 19% higher for the
company. But for a 15-year project,
difference zooms to 69%. So Japan's
h-praised willingness to invest for
long haul and America's apparent
ssion with the short-term may large-
reflect different capital costs rather
cultural preferences.

apan's low interest rates and boom-
stock market in the 1980s translated
a huge increase in business invest-
t. For example, between 1987 and

country to another, eliminating any per-
sistent real interest-rate disparities. U. S.
corporate treasurers are also more
adroit at raising money overseas if there
is an advantage to exploit. The growing
integration of the world capital markets
may help explain why Japanese invest-
ors are beginning to demand higher re-
turns these days, says James M. Po-
terba, an economist at Massachusetts
Institute of Technology.

To be sure, even as interest rates
and equity valuations move closer to-
gether, some economists maintain that
Japanese and German competitors will
still have an advantage in raising long-

AMERICA IS NO LONGER HANDICAPPED



, investment rose by 51% while U. S.
ness investment increased by 15%.
now that Japanese interest rates
e shot up and its stock market has
ed, capital investment should rise by
3.1% through March, 1992, says
mit L. Schoenholtz, an economist at
mon Brothers Asia Ltd. in Tokyo.
hy are capital costs converging
? For one thing, U. S. inflation rates
e been steadily moving down, getting
er in line with German and Japanese
s—two historically low-inflation
tries. For another, the U. S. econ-
is recovering and corporate profits
expected to rise smartly. Combined
lower inflation, the recovery is fuel-
a bull market in stocks, which lowers
tal costs.

TING BILLIONS. Perhaps as important
ne new world of global capital mar-
. On the borrowing side, interest
markets around the world are in-
singly integrated. Investors, armed
round-the-clock computerized trad-
systems, can shift billions from one

term capital. U. S. companies rely on a
diverse pool of market investors for
most of their outside financings. In Ja-
pan and Germany, significant cross-own-
ership of shares among affiliated compa-
nies and especially banks creates a
stable source of capital. These foreign
investors are willing to wait longer for
paybacks than are many American in-
vestors. They are also expected to resus-
cite troubled companies rather than
throw them into bankruptcy.

Nonetheless, the building blocks for a
more competitive era for the U. S. are
falling into place. In addition to cheaper
capital, labor costs are now among the
lowest in the industrialized world. Amer-
ican manufacturing productivity is up
some 40% since the early 1980s. Amer-
ican exports are strong, and the trade
gap is narrowing. The 1990s may just
turn out to be the decade when the rest
of the world begins to worry about
America's new economic muscle.

*By Christopher Farrell in New York,
with Ted Holden in Tokyo*

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THE CLASS ACTION AGAINST PRODUCT-LIABILITY LAWS

Business claims its campaign for an overhaul is gaining momentum

Harry E. Featherstone is fed up with fighting customer lawsuits. The CEO of Will-Burt Co., a machine-parts maker based in Orrville, Ohio, says his company rarely loses in court. Even so, Featherstone is shunning the litigious U.S. market. He's planning to sell the latest version of Will-Burt's premier product, an electronic tower used by mobile television crews for news gathering, only in Britain. That way, he can avoid suits in the U.S. And if he does go to court, the British rules are far friendlier to corporate defendants than those here.

Featherstone's decision is just the kind of horror story business groups love to tell when urging an overhaul of U.S. liability laws. "Our product-liability system discourages innovation because of unforeseeable potential liability costs," said FMC Corp. CEO Robert H. Malott, who chairs the Business Roundtable's product-liability task force.

For more than a decade now, business has lobbied Congress to stop the flood of multimillion-dollar verdicts and punitive awards. It wants to replace the patchwork of state product-liability laws with a uniform federal code. But year after year, business has been quashed by an even stronger front: consumer groups led by Ralph Nader and the pro-

plaintiff Association of Trial Lawyers. They have argued that the threat of suits and megaverdicts forces companies to make safer products.

Now, the skirmishing over liability reform is shifting in ways that buoy business' cause. New evidence suggests that the system doesn't work the way consumer groups claim. And there's pressure, from judges and the White House, to unclog the courts. The stakes are

high. Each year, over \$100 billion flows through the liability system from companies to lawyers and claimants.

The latest test is set for July 24, when a business-backed reform bill will be introduced in the House. A similar bill boasting 35 co-sponsors is in the Senate. **ONE VOICE.** The bills include such perennial provisions as punitive-damage curbs and limits on pain-and-suffering awards (table). But other sections promote settlements. One such provision will force parties who reject settlement offers and are awarded less money at trial to pay some of their opponents' legal bills. The business lobby claims the provision is pro-consumer because it encourages speedier payouts. But consumer groups say it would deter people from suing.

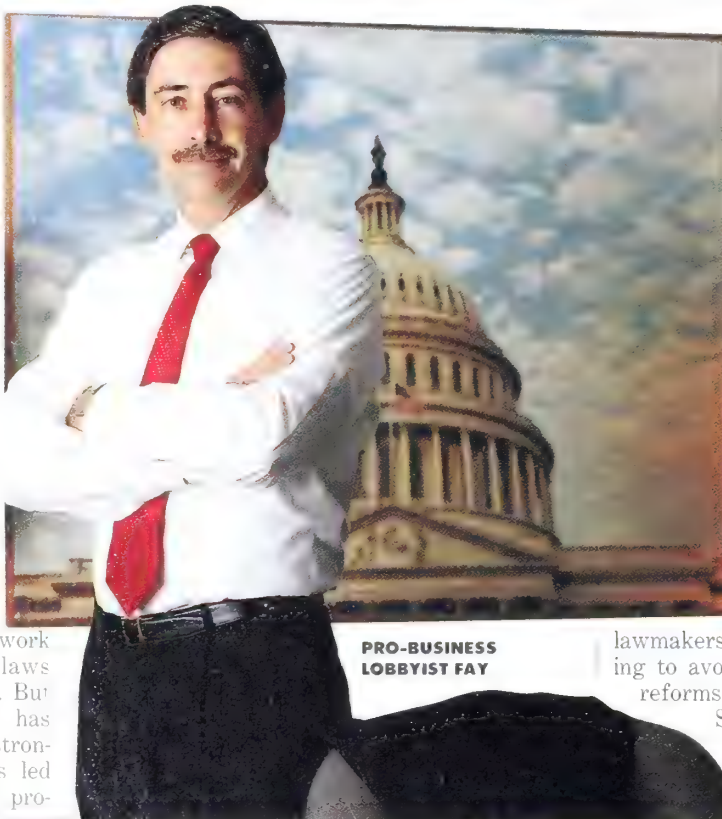
While a federal liability law isn't likely soon, the well-heeled business lobby says it's gaining momentum. Through the four-year-old Product Liability Coor-

ordinating Committee, which represents some 700,000 companies, business is speaking with a single voice. It's also stepping up its assault. In March, the committee hired veteran lobbyist William D. Fay known for his skillful efforts on behalf of the pro-business Clean Air Act coalition. Fay shrewdly backed the goal of clean air—but attacked the high societal costs of the environmentalists' aims. The strategy, he says, got business "a lot better deal."

Fay is using similar tactics in his product-liability fight. He is wooing both houses of Congress and reaching out to consumers. Fay hopes to convince

lawmakers that business isn't just trying to avoid suits but seeks reasonable reforms for consumers, too.

So far, consumer groups are unimpressed. "In clean air Fay's efforts weakened consumer protection by weak-



PRO-BUSINESS LOBBYIST FAY

HOW TO STOP THE STAMPEDE OF LAWSUITS—A WISH LIST

DATA: BW, AMERICAN TORT REFORM ASSN

CURRENT SITUATION

- ▶ Patchwork of state laws
- ▶ No statutory limits on punitive damages in most states
- ▶ Meeting government standards is no defense in most states
- ▶ Victorious plaintiffs in about 30 states can collect full damages from any defendant, even if the company is only partly at fault

WHAT BUSINESS WANTS

- ▶ Uniform federal code
- ▶ No punitive damages unless plaintiff meets tougher standard of proof
- ▶ Absolute shield from punitive damages for drugs, medical devices, and aircraft that meet with government regulations if no fraud
- ▶ Victorious plaintiffs can recover damages only to the extent defendants are liable



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ening government oversight. In product liability, they're weakening consumer protection by restricting the legal system," says Pamela Gilbert, a lobbyist for Nader's Congress Watch. Gilbert is confident of whipping business because, she says, there's no proof that the liability system is out of control. She cites a recent Rand Institute for Civil Justice finding that only about 1 in 10 accident victims considers suing.

IDEA-BUSTING? Still, business has potent weapons of its own. A new Brookings Institution book, entitled *The Liability Maze*, studied the impact of suits on safety and innovation in five industries: autos, chemicals, private aircrafts, pharmaceuticals, and the medical profession.

For some chemical hazards, the liability system offers modest safety incentives, the book says. But for the rest, litigation "doesn't seem to be the overwhelming driving force for safety," says co-editor Robert E. Litan. More important factors are government regulation and fears that bad publicity will drive away customers. And the book leans toward one of business' key claims—that the uncertainty over damage awards "has probably reduced innovation."

Lawmakers also face pressure to help business from the Bush Administration. In August, its Council on Competitiveness is aiming to unveil plans for overhauling the courts. "The entire system has become fraught with excess cost and delay," says Solicitor General Kenneth Starr, who heads the council's working group on civil justice reform.

One of its goals is to make the U.S. legal system more like Europe's. Many European countries bar punitive damages, contingency fees, and class actions. While the council is still readying its final proposals, it will likely suggest forcing losers to foot their opponents' legal bills. Fee shifting is popular in Britain and other countries.

Even legal groups are pushing liability reform. In April, the prestigious American Law Institute released a five-year study that urges sweeping changes—and offers a blueprint. The plans include letting courts create giant class actions to handle asbestos claims.

Business already has had success persuading state lawmakers to write friendlier liability laws. But business and consumer groups remain far apart on federal reform. One thing they can agree on—the need to cut the agonizingly long wait for cases to end. Still, the necessary compromises seem far off.

Until then, Featherstone is taking matters into his own hands. Come fall, the 62-year-old is starting law school. The CEO spends so much time in court, he might as well get paid for it.

By Michele Galen in New York, with Tim Smart in Washington

Marketing

DEMOGRAPHICS

HOME ALONE— WITH \$660 BILLION

Single Americans are turning into a marketer's dream

Met David Freeman, single. A prospering freelance journalist, Freeman, 32, has the kind of unencumbered cash flow and hedonistic tastes that make marketers drool. Freeman spends \$150 a week eating out or ordering in. He stays in shape by riding his \$600 Cannondale bicycle in biathlons. He takes such "adventure" vacations as scuba diving in the Caymans. His New York apartment is crammed with a VCR, two TVs, a fancy stereo, and a personal computer.

He may be single, but Freeman's not alone. The 1990 census shows that about 23 million Americans live by themselves, a 91% jump for women since 1970, and a 156% increase for men over the same period (chart). Two trends are behind this singles surge. Says Neil Bennett, an associate sociology professor at Yale: "Unprecedented numbers of (adults) are never marrying, and by some estimates, 60% of all couples divorce."

TOUGH MARKET. According to Peter Kim, U.S. strategic planning director at ad agency J. Walter Thompson Co., middle-aged singles are among the fastest-growing of these groups. But Kim points out the market is even larger than these numbers suggest. Some 18 million adults aged 18 to 34 live with their parents or in college dormitories and have plenty of spending money. Throw in these other singles and Kim estimates the group has an earning power of \$660 billion. And as married baby boomers evolve into budget-conscious parents, the affluent singles may prove to be the last big spenders.

It's an attractive market, but a tough one. Studies show singles share such traits as a tendency to spend more on travel, convenience foods, and restaurants than married adults. But this vast, fragmented group includes everyone from carefree 21-year-olds to elderly

widows. Then there's the delicate task of getting a message across without offending. As Jane R. Fitzgibbon, a group director at Ogilvy & Mather Advertising puts it, too often marketers have been "treating singles as if they were just some sort of extramarital aberration."

Campbell Soup Co. made that mistake with its Soup for One line. "Our consumers told us Soup for One is a lonely name. They are eating alone and they don't need to be reminded," says Robert Bernstock, a vice-president in the soup division. In 1990, after years of mediocre sales, the Soup for One label was removed. Single-serving sizes now come without the offending label, and Bernstock reports improved sales.

Other marketers with appeals that are apparently aimed at singles don't like to talk about it. A print ad for Häagen-Dazs ice cream has a woman finding her ice cream bar more appealing than



boyfriend's conversation. Sounds like a pitch to singles, right? Nope, in Yves Coleon, vice-president for marketing: "We are not making a conscious effort to go after singles." He, though, that Häagen-Dazs ice cream "is a high-indulgence food that really appeals to singles who are a little price-sensitive."

HAPPY. Many companies, however, do admit to chasing the unattached. Ask MCI Telecommunications Corp. Timothy F. Price, senior vice-president for marketing at MCI: "Single people don't have nuclear families. So they're more emotionally connected to family and friends elsewhere. That's why high phone usage." MCI covets customers such as Elaine Dimond, a 53-year-old publishing executive with two teenage children. Dimond spends \$100 to a month on long-distance calls. "I spend a lot on the phone to make up for my types of entertainment," she says. To reach the dial-happy, MCI does not use the word 'single' in its singles-oriented campaigns. Instead, several "Friends and Family" ads show attractive adults varying ages in nonfamily settings making lists of friends to phone. If customers get friends and family to join MCI, then, both parties get 20% discounts on calls made to each other. Some industries that often ignored singles are now courting them. John, a 55-year-old divorced disk jockey, says traveling is a problem "because a person is charged for not having a companion." To

attract customers such as Bell, Hyatt Hotels Corp. tested a "Single Share" program at its Beaver Creek ski resort in Colorado last winter. Hyatt provided roommates, and thus reduced room rates, to people traveling alone. If Hyatt couldn't find a roommate, singles still paid half price. Hyatt will expand the program this winter.

Some companies are appealing to young singles. Saturn Corp., a unit of GM, recently put up billboards in California showing a snazzy two-door Saturn with a caption that reads like a personal ad: "Single, bright, and available." Says Thomas W. Shaver, Saturn's director of consumer marketing: "If we can catch people early when they're single, maybe we'll have a long-term relationship."

Other marketers want older singles. Last year, Colgate ran a TV ad showing a 40-year-old single mother of two brushing her teeth while getting ready for her first date in years. Royal Cruise Line, which caters to an older crowd, has a successful program that gets men over 50 to act as dance partners and social hosts to single women. Says a spokeswoman: "Travel agents at first



thought we were putting gigolos on the ships, but we have strict screening procedures. These men are not paid so they must be men of means."

Despite all the activity, many singles markets remain largely unexploited. Take financial services. "The next generation of investors is going to be unmarried women who have legitimate financial needs," says Richard Hokenson, de-

mographer at Donaldson, Lufkin & Jenrette Securities Corp. But, he says, banks typically target men and multiperson households with income of \$75,000 or more, and miss the single women making \$50,000 or more a year.

Other companies serendipitously discover singles. For the IBM PS/1 personal computer, the first ad line "IBM brings it home" targeted families. But when marketing manager Skip Gladfelter found that many PS/1 buyers were young and probably single, he switched to individual testimonials. Says Gladfelter, "We've stopped precluding singles." Including, not excluding, this group could be a singularly shrewd strategy.

By Laura Zinn, with Heather Keets in New York, James B. Treece in Detroit, and bureau reports

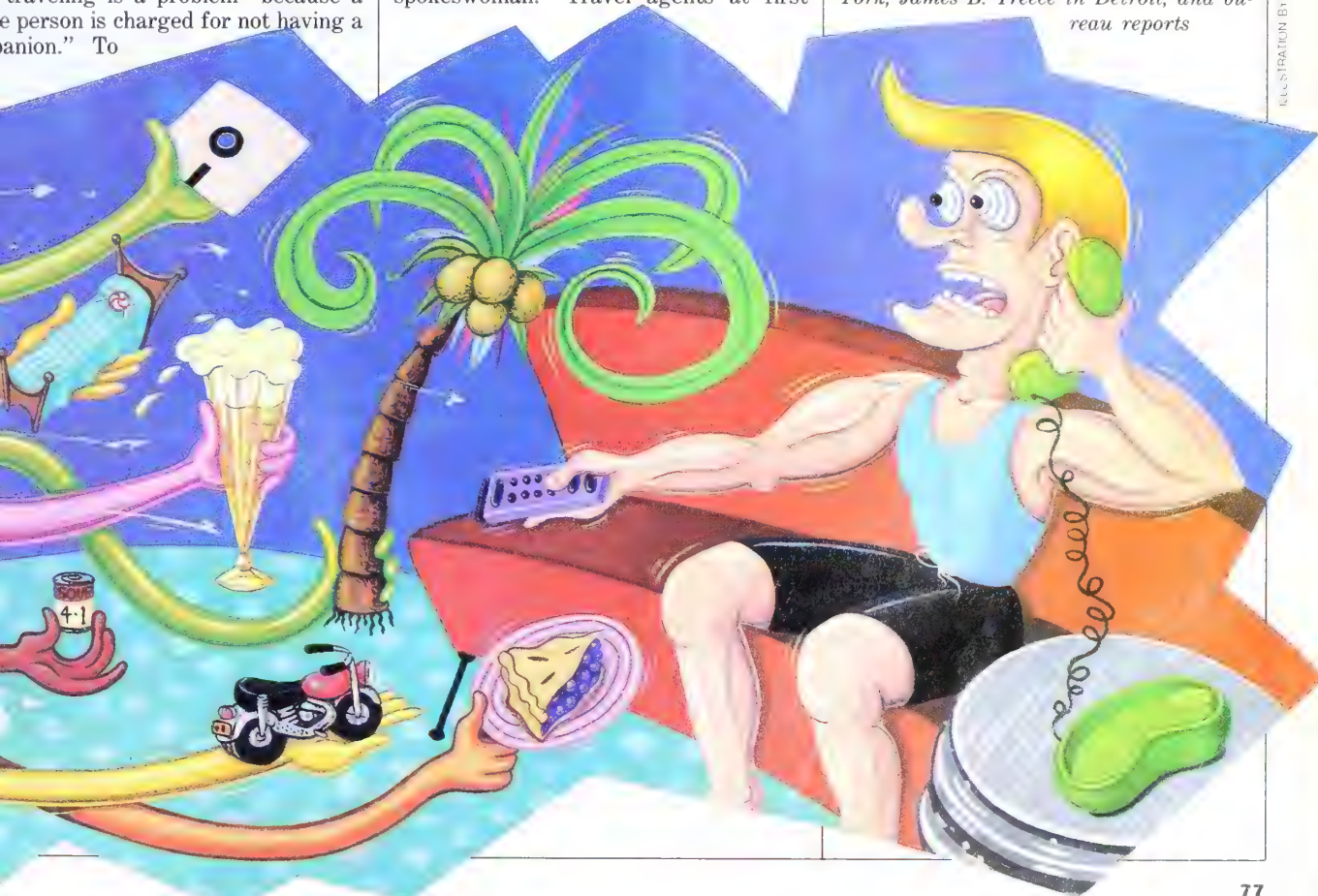


ILLUSTRATION BY MIRE FANTUSO. CHART BY RAY VELLA BIV

CONFESSIONS OF A COMPULSIVE HIGH-ROLLER

What's the difference between a casino gambler and a risk-taking entrepreneur? Not so much

One summer day in 1975, Bernie Frederick had such a hot hand it nearly melted. The New York lawyer, a heavy gambler who was then under indictment for his role in a stock swindle, had come to Las Vegas with \$17,000 in racetrack winnings. Sitting down at the blackjack table, Frederick—a pseudonym chosen to protect his identity—pulled out two \$100 bills and over the next six hours ran up a gain of \$56,000. Gambling straight through dinner in a special room for high-rollers, he won another \$20,000. After dessert, he tallied an additional \$18,000. "Now I've got \$111,000," he recalls. "I put it in a safe-deposit box and go to bed happy. Back home I have huge legal fees, and my mortgage is going unpaid, but this money will straighten everything out."

Wanna bet? Unable to stay in bed, Frederick marched back down to the lobby and set about gambling again. By the time he slunk out of the casino four hours later, he had blown his entire winnings. In fact, he was in the hole to the casino for \$25,000. "Flying home, I finally realized I was sick," says Frederick, now 48. "No matter how much I won, it would never be enough."

PAINFUL LESSONS. This is the story of a compulsive gambler who put his life back together. After spending three months in federal prison because of the stock swindle, Frederick dived headfirst into entrepreneurship and in 10 years built a publicly traded service business with sales of nearly \$100 million. "My message is, no matter how much trouble you're in, there's always hope," he explains, leaning over a cluttered desk in his airy New York office. "You can turn it all around once you give up gambling." But along the way, Frederick learned some painful lessons about his compulsive personality and about the uneasy relationship between gambling and entrepreneurship.

Although he hasn't made a bet in 16 years, the traits that made him a destructive gambler still haunt him—and affect the way he does business. Three

years ago, after acquiring a string of \$10 million companies, Frederick went for broke and bought a company in a related field with \$50 million in sales. It was too much, and he now operates his much smaller business under Chapter 11 bankruptcy protection. The risky takeover may not have been gambling in the racetrack or casino sense, but in Frederick's case, it was still a craps shoot. "I would have been happy with the business he had going," says Ann, his wife of 20 years. "He wanted more. That's his personality."

There are lots of people like him. Frederick's gambling addiction is shared by an estimated 12 million people in the U.S., and that number is growing every day. Americans bet \$286 billion legally last year, or more than twice the 1982 level, figures *Gaming & Wagering Business* magazine. Arnie Wexler, executive director of the Council on Compulsive Gambling of New Jersey, sees no end in sight. With states continually legalizing more forms of betting, from lotteries to bingo to riverboat gambling, "we're building a nation of gamblers," he warns. "A lot of people are going to get destroyed."

Frederick does not seem like an obvious candidate for destruction. Tall and energetic, he darts around his offices with an air of considerable self-confidence. Joking about the travails of small businesses in a deep, distinctly New York voice, he conveys street-smarts not found in many corporate suites. "The thing about compulsive gamblers is, it's impossible to tell who they are," says Edward Looney, a counselor at the John F. Kennedy Medical Center in Edison, N. J. "Usually, they're the kind of people

who have lots of friends on the outside but are very lonely inside."

Frederick traces his love of gambling back to elementary school, when he stole quarters from his mother's change purse to make small bets on baseball games. By high school, he had discovered cards; in college, he found bookies and horse racing. Soon after graduating from law school and opening a small firm with a partner, he paid his first visit to a glittering casino.

From then on, he always made sure to take vacations in places where he could gamble, such as Las Vegas or Monaco. It didn't matter what the game was, or even if he knew the rules. In France, he once tried a game called *vingt-trente* or twenty-thirty. "The guy would flip down three cards: 'Un, deux, trois. You lose. Un, deux, trois. You lose.' I sat there for an hour!" But then, the money no longer mattered. When he won a bet, "it just felt so good to be right," he explains. "It's a feeling of euphoria, not money."

STRAINS AT HOME. Still, you're going to be a high-rolling compulsive gambler, you need a lot of money. So Frederick began to break the law. His

main money-making technique was the stock swindle. Typically, he would get his hands on a block of shares in a penny-stock company, then pay off five or six brokers to bid up the price. He made millions of dollars per scam, he says, and he pulled dozens of them. He was caught a few times and sanctioned by the Securities & Exchange Commission but that didn't stop him.

In fact, he only got worse. In the mid-1970s, he joined a group of alleged mobsters in a crooked real estate scheme

"I know I was doing bad things. I was a liar and a thief. But the monkey was on my back, and I needed a fix."



ly, Frederick tripped himself up by giving some penny-stock investors who went back. A U.S. Attorney got involved and put him behind bars. "I knew I was doing bad things," he recalls. "I was a liar and a thief. But the monkey was on my back, and I needed a fix." Frederick's gambling had ugly effects on his wife and two young children, when he did come home, he was in a rage over losing a bet. Wife

(also a pseudonym) told him to quit. He told her to leave him alone, that it was under control. "I felt I was the problem," Ann says. "I thought I was having a nervous breakdown."

THE STEPS. Days after his painful last trip to Vegas, Frederick's family persuaded him to join his first Gamblers Anonymous meeting. Among the program's hallmarks are helping gamblers to realize they can't control their gambling; helping them work out a payment schedule to wipe out their debts; and a 12-step program of recovery patterned after Alcoholics Anonymous. It takes three or four years before the urge to gamble disappears. Frederick attends a GA meeting every week. Out of gratitude to the program, Ann still handles the family finances—the GA stripped from Frederick 15 years ago. Five months after joining the GA program, Frederick went off to prison. It wasn't bad, he says, because he knew he couldn't be there for more than three months. When he came out, he saw the more lasting punishment he had

Long hours and \$200,000 in seed money, obtained from a group of lawyers and other professionals who knew all about his past, paid off in a big way. Frederick's company went public in the mid-1980s, and its stock soared. His net worth topped \$20 million, and he was written about glowingly and at great length in a major business magazine.

The magazine didn't know about Frederick's gambling addiction or his felony conviction, but he had notified the SEC

ited. But even that had its dangers. Before long, he had become a true workaholic and could barely tear himself away from the office. Finally, he and Ann worked out a deal: He takes a full eight weeks of vacation every year, plus he skips out on Friday afternoons in the summer. "Compulsiveness is something I have to fight every day," he says. He was even hooked on cocaine for a year while in Gamblers Anonymous. And he will order only one drink when dining

out, knowing that he'll have trouble stopping if he has more than one.

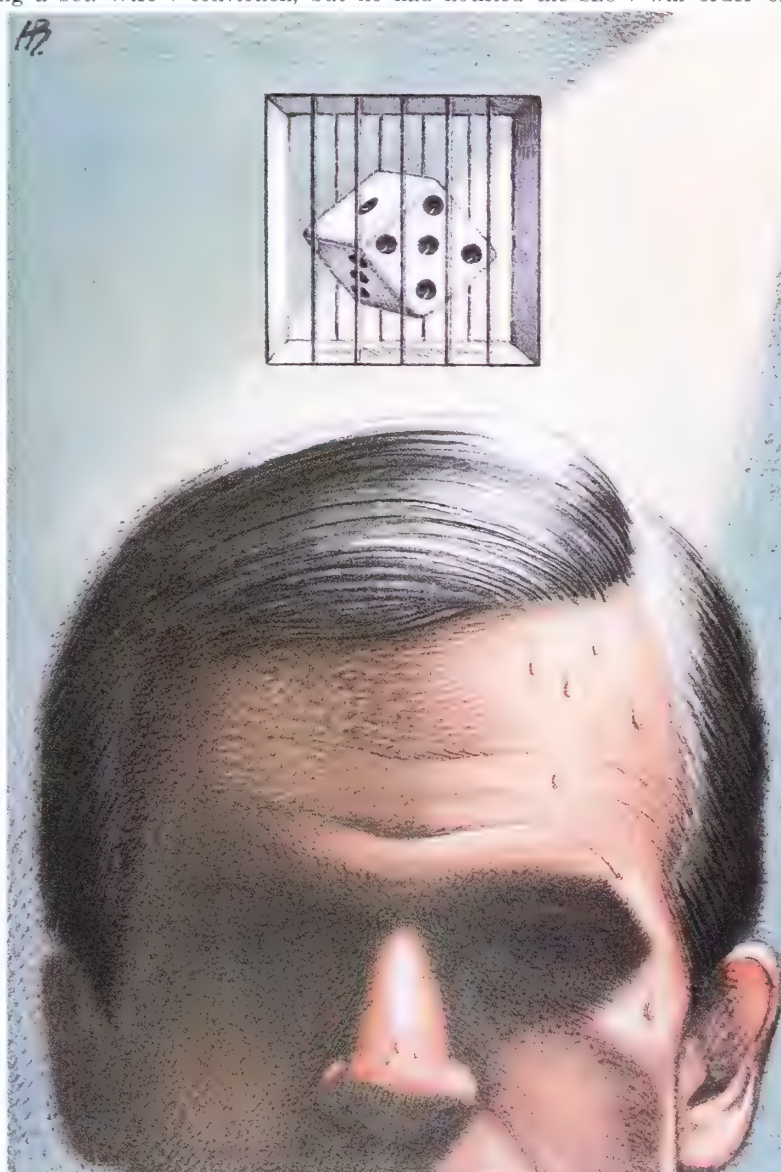
Those sensible rules were more difficult to apply when it came to running his business. Frederick built his company through the roaring '80s with a series of timely acquisitions. But the last—and biggest—company he bought was heavily in debt and bleeding cash. Still, he had paid next to nothing for it, and he was sure he could turn it around. Instead, about a year later, it went down and dragged Frederick's company along with it.

NEVER FREE. Today, his company is moderately profitable, the reorganization is on schedule, and his lawyer says he'll be out of Chapter 11 by October. Already, Frederick is bubbling over with ideas for new ventures. But he will never be free of his compulsion. He still has dreams about gambling sometimes. And then there's the question he would like most to avoid: Is his bold style of doing business an extension of his gambling addiction? Frederick winces at the idea. Business risks, he argues, are a far cry from gambling because

he has some control over the outcome. "My goal was always to get the business to \$100 million in sales," he says. "I don't think that's the same as gambling, but I guess somebody else might look at it differently."

Yet, after a long pause, he concedes that the distinction between gambling and risk-taking is something he has been thinking about a lot lately. More than likely, he'll be thinking about it for the rest of his life.

By Peter Finch in New York



and he wasn't keeping it a secret from his lenders. Most were surprisingly understanding, he says. He did get some funny reactions, though. Once, at the end of a presentation for potential investors at a brokerage, an executive asked if there was anything else he had to say. "I said, 'Well, I was in a federal penitentiary . . .'" One guy actually dropped his fork onto his plate—clink! I looked up, and everyone's jaw had dropped."

Frederick found that entrepreneurship filled the void that gambling once inhab-

Planning

THE PITFALLS OF LOANS FROM THE HEART



In these times of tight money, the family is often the only "bank" willing to finance that

first home or new business. But throwing a child or relative a monetary lifeline is not as simple as writing a check. You have to avoid tangling with the Loan Ranger—the Internal Revenue Service.

Suppose you want to lend your daughter the \$45,000 downpayment on a handyman special. You have two decisions to make: whether to make an unsecured loan or one secured by a mortgage or trust deed on the house, and whether to charge interest. You can make an interest-free loan without it necessarily being considered a gift. But, as you'll see later, you probably won't want to.

NO SECRETS. Some parents worry that taking a second mortgage will alarm the first lender and make it harder for their children to qualify for other loans in the future. To try to keep the downpayment loan a secret, they don't ask for collateral. That is a mistake.

No matter how much you trust your children, you should protect yourself against possible calamities, such as their divorce, disability, or death. Also, the first mortgage holder has a legal right to know about any loans you make. It can call in the first mortgage if the second is discovered.

You are also playing into the hands of the IRS. As the

lender, your taxes are the same whether or not you hold a mortgage—and you must report any interest on the loan as ordinary income. But the interest your child pays on an unsecured home loan is not deductible. True, the money is going to purchase a home, but home interest is deductible only if a loan is secured by the home itself.

What if a relative borrows money to start a business or pay medical expenses? Then the security for the loan has no tax effect. Interest is fully deductible if the loan is spent on business or investments—up to the equivalent of the income generated—and non-deductible if used to pay personal expenses. Again, any interest you receive is taxable.

So should you charge interest? You might as well. If you

and into a warehouse. You decide to spare him the 9% AFR. By making an interest-free loan, you are forgoing \$5,400 in interest each year. And the IRS treats that as a \$5,400 gift to your son.

The gift is less than the \$10,000 that one person can give a relative, so there's no gift tax. But you may owe income tax on the forgone interest. If your outstanding loan is \$10,000 or less and the relative did not use the money to buy or carry stocks or other income-producing assets, you're safe. And if the loan is \$100,000 or less and the relative has less than \$1,000 in net investment income, you're also safe.

SHIFTING INCOME. Going back to the example, you will not have to pay taxes on the \$5,400 of forgone interest if your son has net investment income of less than \$1,000. In that case, a low- or no-interest loan is a good way to make a short-term gift without the bother of setting up a trust.

But if he has investment income of \$3,500, say, you must include \$3,500 in income on Schedule B, form 1040, even though you never pocket a penny of it. Your son may deduct the same \$3,500 as a business expense. Each of you must report the other's name and Social Security number on your return.

The purpose of this elaborate accounting is to keep relatives in lower tax brackets from earning interest on money borrowed from higher-bracket relatives. Shifting income to avoid taxes is still legal, but thanks to the tax

THE LEAST YOU CAN CHARGE FOR FAMILY LOANS

APPLICABLE FEDERAL RATES*

60 YEARS	6.7%
65 YEARS	8.0%
70 YEARS AND UP	8.4%

*For July, 1991; changes monthly

DATA: INTERNAL REVENUE SERVICE

charge no or below-market interest, you're treated as if you received the going rate anyway. The IRS sets a minimum rate for loans between related parties—the Applicable Federal Rate—that changes every month (table). If the difference between the interest you charge and the AFR is more than \$10,000 per year, you may owe gift tax.

Say you lend your son \$60,000 to move his mail-order business out of the garage

law, it's seldom profitable

Because the IRS scrutinizes family loans the way you sniff week-old milk, it's important to take a businesslike attitude. That means having an enforceable note, which shows a fixed loan amount, definite payment date, a stated rate of interest, and collateral or security. One important condition: Repayment can't be made contingent on the borrower making a profit.

Keep in mind that over the years dismayed taxpayers have seen many family "loans" ruled as gifts. They include money borrowed by:

■ A husband from his wife





his medical education, though he signed promissory notes.

brother-in-law to pay alimony to the taxpayer's sister. An aged aunt and uncle, and in failing health—these assets were clearly insufficient to make repayment. The mother, age 70, who had a no-interest note due years later.

child under 18 years old pay for necessities.

that constitutes a "sham," resulting in loss of tax benefits.

This did: A father gave \$60,000 to a child, then borrowed back the money and repeated the process with the

same \$5,000 for each of his other four children—solely to create interest deductions.

But not this: A dentist borrowed money from his parents to buy a townhouse. He gave them a promissory note at 12% interest and made each scheduled payment. The same year, his parents moved into the townhouse. They paid rent at fair-market value, and the son kept a separate bank account for the property. The district court said the loan was commercially sound and the property was managed as a business, not as a tax-avoidance scheme.

IRS skepticism about whether

your debt is bona fide can dent your pocketbook. Take that \$45,000 downpayment loan to your daughter. If you can't convince the IRS it's a loan, you'll be hit with gift tax on the amount over \$10,000 (\$20,000 if you are married).

You also stand to lose the deduction for bad-debt losses if the loan is not repaid. Suppose your son's minimal business goes belly-up shortly after he sinks your \$60,000 into display cases and advertising. If you can prove a valid debt, you may deduct the entire \$60,000 as a short-term capital loss on Schedule D, form

1040. If the IRS calls it a gift or a contribution to capital, you lose not only your \$60,000, but the deduction too.

What if your relative files for bankruptcy? Make sure you are listed as a creditor. And don't lend any more money. Cash advances made after a relative becomes insolvent are gifts. If you're tempted to cancel the debt, remember that the amount of any debt forgiven is also a gift.

The better part of wisdom in drafting a family loan is to consult your tax adviser first. That way, your good intentions won't run afoul of the IRS.

Mary Sproule

Autos

TWO COUPES WITH CACHET TO SPARE

Cruising in the fast lane keeps getting cushier. Two pacesetting luxury coupes hit the road this year: the Lexus SC400, made by Toyota, and the BMW 850i. Each is lightning-quick, but they differ in character and cost. The Lexus is less than half the price of the BMW, which starts at \$85,470, including luxury and gas-guzzler taxes. That helps make the SC400 a better value, but the BMW has snazzy features that the Lexus can't match.

The Lexus is curvaceous and sexy, with a design that seems to invite caressing. The BMW is striking, too, but in a more functional manner. It's a low, wide wedge with angular lines that evoke a sense of power rather than sensuality.

On the road, they also vary more in style than substance.



The Lexus SC400 (red) at \$38,250 and the BMW 850i (silver) at \$85,470 both romp to 60 mph in less than seven seconds

Both cars romp to 60 mph in under seven seconds. Their automatic transmissions make silky-smooth shifts. (The BMW is also available with a six-speed manual.) Antilock disk brakes stop the cars quickly and precisely. Despite uncanny cornering, both coupes soak up bumps easily.

The 4,123-pound BMW has a 296-horsepower V-12 under the hood. The Lexus uses a 250-hp V-8. But the smaller engine still launches the car with a whoosh, since the

SC400 is 550 pounds lighter. And the coupe feels nimbler than its cousin, the bigger, statelier LS400 sedan.

OVERLOAD. Technology buffs will love the BMW's whiz-bang features, which include automatic traction control during high-speed cornering and windows that seal automatically when you close the door, for better aerodynamics. Cellular phone and CD changer are standard, too.

But the gizmos on the 850i dashboard approach overkill.

Especially confusing is the trip computer, which displays everything from the outside temperature to how many miles are left in the gas tank. The Lexus dash is more simply laid out and easier to read.

The SC400 starts at \$38,250. Add traction control, a sunroof, and a stereo with 12-disc CD changer, and the price rises to \$43,420. If you think that's pricey, a fully loaded BMW hits \$89,837. Who ever said life in the fast lane came cheap?

David Woodruff

The Age of the Lawsuit has brought new urgency to the problem of protecting personal assets in case of a business disaster. In the old days, professionals who feared malpractice or liability suits incorporated themselves. But courts are increasingly letting creditors and litigants get past the corporate shield. Insurance has grown wildly expensive in response to the litigation explosion and often doesn't cover punitive damages.

Now, financial planners have devised a new solution. It involves setting up a limited partnership using the assets you want to shield, then putting a portion of them in trust in a country where asset-protection laws are more favorable than in the U.S. Such commonwealths as the Isle of Man and the Cook Islands, for example, have strong statutes that prohibit litigants from "piercing" a

Smart Money

BARRICADING YOUR ASSETS BEFORE YOU'RE SUED

trust to recover funds, no matter what the liability.

Say you want to protect a stock portfolio. By creating a limited partnership with yourself as general partner, you retain control of the investments. But you take only 1% interest in the partnership, transferring the other 99% to the international trust. Although you continue to manage the money, 99% of it remains untouchable—either by you or creditors. As with any trust, you specify when the funds become free—say, after retirement.

The plan works best when it's set up before you get into trouble, says Alan Jahde, a director of law firm

Boris, Nemkov, Jahde & Frankl in Denver and one of the dozen or so lawyers around the U.S. who have designed such combos. Existing creditors have two years

Foreign trusts are a natural response to the litigation boom

to challenge the trust as a fraudulent conveyance—a phony way of placing assets out of reach. Also, the trust must not leave you insolvent. That stock portfolio should represent no more than two-

thirds of your net worth.

Why doesn't every doctor have such a trust? "Many people just don't like to denude themselves of their assets," says one New York estate-planning specialist. If you can afford the premiums, you may be more comfortable with insurance.

NO BREAKS. Legal fees to set up foreign trusts depend on the size of your estate, starting at around \$15,000 for a \$1 million account. The annual custodial fee is minimal, since you're managing the money. Typically, international trustees charge \$750 to \$1,500. Both your lawyer and financial planner should design the limited partnership and foreign account.

A foreign trust can't be used to protect pension assets. And it's no tax break: You must report all income to the IRS. But if set up right, it can be virtually impenetrable.

Joan Warner



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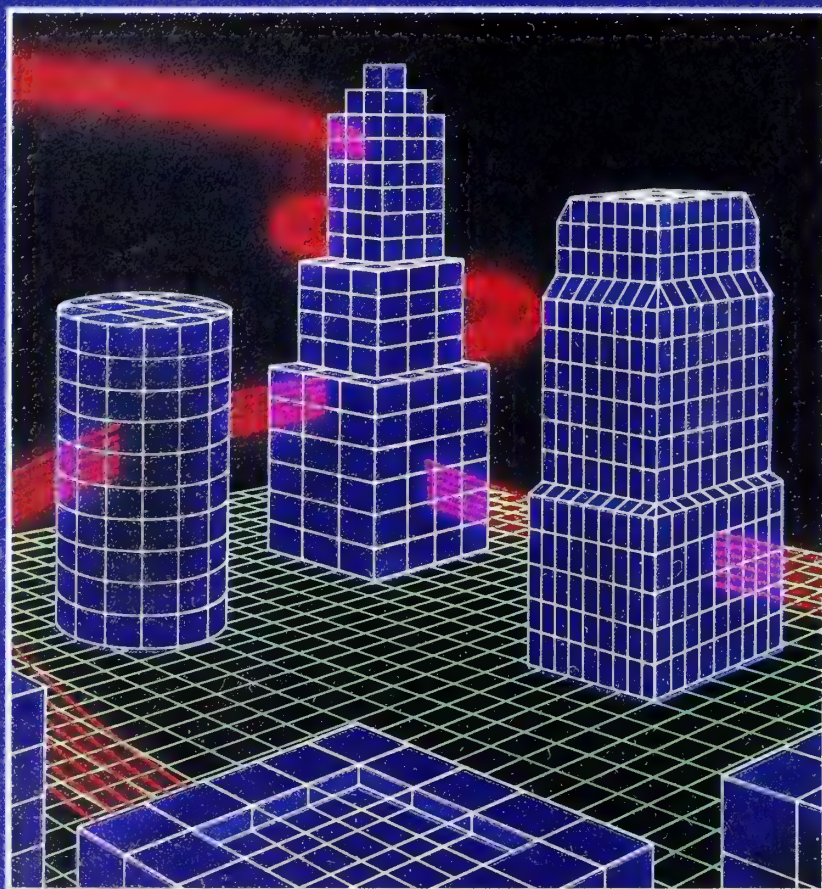
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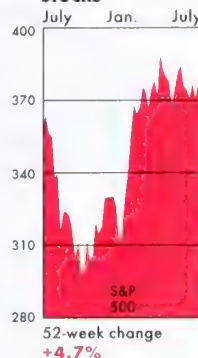
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Investment Figures of the Week

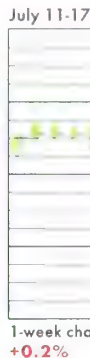
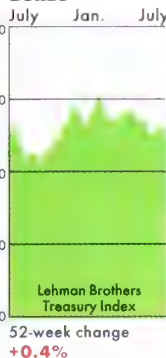
STOCKS

by an improving economic outlook and the announced merger of New York banks, the Dow Jones made another rush to 10,000. But the rally couldn't be sustained. Disappointments on quarterly earnings are hurting the stock market, where interest rates are keeping rates only high. June's Consumer Price Index was above expectations and oil prices are at the point since the start of the Gulf war in January.

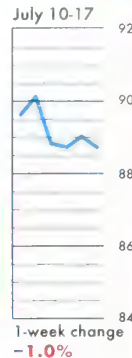
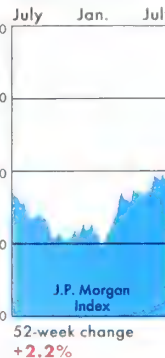
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

	Latest	% change Week	% change 52-week
INDUSTRIALS	2978.8	1.2	-0.1
COMPANIES (Russell 1000)	199.3	1.4	5.4
COMPANIES (Russell 2000)	171.3	1.3	2.1
COMPANIES (Russell 3000)	211.7	1.4	5.2

	Latest	% change Week	% change 52-week
FINANCIAL TIMES 100	2561.0	2.1	6.6
NIKKEI INDEX	23,060.7	-0.3	-30.2
TSE COMPOSITE	3541.8	1.1	-1.1

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.8%	5.7%	7.8%
30-YEAR TREASURY BOND YIELD	8.5%	8.5%	8.6%
S&P 500 DIVIDEND YIELD	3.2%	3.3%	3.2%
S&P 500 PRICE/EARNINGS RATIO	18.7	18.4	16.7

TECHNICAL INDICATORS

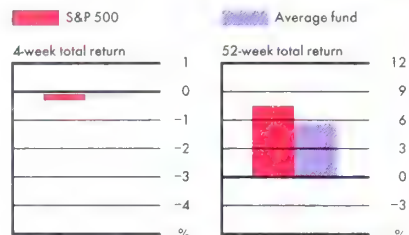
	Latest	Week ago	Reading
S&P 500 26-week moving average	371.3	368.8	Positive
Stocks above 26-week moving average	57.7%	56.2%	Neutral
Speculative sentiment: Put/call ratio	0.47	0.48	Positive
Insider sentiment: Vickers sell/buy ratio	3.02	2.96	Negative

INDUSTRY GROUPS

WEEK LEADERS	% change		Strongest stock in group	% change		Price
	4-week	52-week		4-week	52-week	
ES	10.1	16.1	STRIDE RITE	13.4	77.4	51 ⁷ / ₈
UMENTATION	7.7	19.4	HEWLETT-PACKARD	9.0	17.7	55 ³ / ₄
UALITY APPAREL RETAILERS	6.6	44.2	GAP	7.7	103.8	66 ¹ / ₄
ING	6.4	10.9	MIRAGE RESORTS	7.3	-26.2	27 ¹ / ₂
D MINING	5.8	-12.7	HOMESTAKE MINING	9.2	-3.4	17 ³ / ₄
WEEK LAGGARDS	% change		Weakest stock in group	% change		Price
	4-week	52-week		4-week	52-week	
.	-8.9	-11.0	PITTSTON	-14.9	-9.5	17 ⁷ / ₈
CKING	-8.7	22.2	YELLOW FREIGHT SYSTEM	-12.4	-0.9	28 ¹ / ₄
URAL GAS DISTRIBUTION	-8.6	-18.6	COLUMBIA GAS SYSTEM	-53.1	-62.0	17
UTION CONTROL	-7.1	-26.3	WASTE MANAGEMENT	-8.3	-19.7	36 ¹ / ₈
GLOMERATES	-6.8	-18.8	TENNECO	-15.6	-48.5	35 ⁷ / ₈

MUTUAL FUNDS

	%	LAGGARDS	%
Four-week total return		Four-week total return	
INTERNATIONAL INVESTORS	8.7	EQUITY STRATEGIES	-8.1
CAPITAL DEVELOPMENT	8.2	FIDELITY SELECT ENERGY SERVICE	-8.0
STRATEGIC INVESTMENTS	8.2	METLIFE-STATE STREET GLOBAL ENERGY	-7.1
52-week total return		52-week total return	
SELECT BIOTECHNOLOGY	51.6	BULL & BEAR SPECIAL EQUITIES	-42.1
SELECT MEDICAL DELIVERY	48.4	STEADMAN OCEANOGRAPHIC TECHNOLOGY	-41.7
SELECT HEALTH CARE	45.8	UNITED SERVICES EUROPEAN EQUITY	-31.8



RELATIVE PORTFOLIOS

	Treasury bonds	Money market fund	U. S. stocks	Gold	Foreign stocks
Amounts					
Present the present					
of \$10,000					
one year ago					
portfolio					
Pages indicate					
total returns					
	\$10,893	\$10,605	\$10,480	\$10,149	\$9,229
	+0.98%	+0.11%	+1.44%	-0.16%	+3.59%

on this page are as of market close Wednesday, July 17, 1991, unless otherwise indicated. Groups include S&P 500 companies only; performance and share prices are as of market close.

July 16. Mutual fund returns are of July 12. Relative portfolios are valued as of July 16. A more detailed explanation of this page is available on request.

TWO-BIT LABS CAN'T MAKE MEGABUCK MATERIALS

The phrase "scientific revolution" may seem trite in an age in which science has accelerated from one astonishing breakthrough to another. But it is an apt description of the advances now being made in materials research and development (page 48).

Using the power of technology developed to deal with the infinitely tiny realms of microelectronics and microbiology, scientists are rearranging molecules and atoms to create entirely new materials and enhance the usefulness of old ones. The results are likely to be felt in all aspects of everyday life—from cars that are big, yet safer and more fuel-efficient, to planes that can hop the Pacific in a couple of hours; from stronger and more resilient bridges and buildings to incredibly light nonpolluting insulation and more lifelike artificial limbs.

The good news is that the U.S. still remains in the forefront of research in many of these areas. The bad news is that it has been losing ground to its competitors. In the past decade, federal funding for materials research has plunged 17% in real terms, while industry support has fallen by almost as much. Meanwhile, Germany and Britain have essentially caught up with the U.S., and Japan has pulled ahead. Although three-quarters of Japan's materials R&D is funded by industry, the nation's powerful Ministry of International Trade & Industry has launched 13 major materials-related projects since 1980.

Commendably, the Bush Administration is starting to face up to the challenge, despite budgetary concerns and a visceral antipathy to industrial policy. Its 1992 budget calls for a new \$84 million materials initiative, and it promises to add hundreds of millions for 1993. But more investment is needed, especially from industry, which has been slow to bring new and improved materials to market.

World sales of electronic ceramics last year topped \$10 billion, and sales of advanced polymer composites hit \$4 billion. The top three suppliers of the former product are Japanese; the top six of the latter are European. By the year 2000, will U.S. companies also be behind in marketing advanced materials that are now emerging from laboratories?

THE DEFECTS IN PRODUCT-LIABILITY LAWS

It's time to face up to the fact that the U.S. product-liability system has itself become a liability to the economy. The current patchwork of 50 state laws is inherently inefficient, raising the costs of litigation as business seeks to comply with diverse legislation and as plaintiffs' lawyers seek the most hospitable venue for claims. Meanwhile, after legal fees and other costs, victims often wind up with only half of the money earmarked for compensation.

Businesses claim that the current liability system is a

hidden tax that is passed on to consumers and dampens U.S. innovation and competitiveness. Stung by the high cost of liability insurance and the unpredictable size of jury awards, they back federal legislation that would replace state laws with a 'uniform liability code. The code would create standards for awarding punitive damages, place limits on pain-and-suffering awards, and exempt new drugs and medical devices that meet regulatory standards from punitive—but not compensatory—damages. Consumer groups oppose such sweeping legislation, arguing that the current system has forced companies to make safer products.

Both sides have legitimate concerns. Recent studies suggest that product-liability laws have indeed spurred some safety improvements. But the uncertainty inherent in the current patchwork of laws has also hampered innovation. And evidence indicates that government regulation and better publicity promote more safety improvements than litigation.

Given the strong opposing arguments, a federal law will not be passed overnight. But it is clearly desirable. Looking forward to economic union, the European Community has already created a uniform liability code that seven nations have adopted. Such a code in the U.S. should set clear standards for punitive damages and provide settlement mechanisms and monetary incentives that could help unclutter the courts. Eliminating the confusion in the current liability system could lower litigation costs for both business and consumers, foster product innovation, and provide injured parties with quicker compensation.

STABILIZE REFORM ALONG WITH THE RUBLE

Of the steps taken by the Group of Seven nations at their London conference, the most important may well be their tentative acceptance of a role for the International Monetary Fund in setting up a mechanism to stabilize the ruble and make it convertible into foreign currencies. Although the Soviets have introduced limited convertibility by holding currency auctions—which have put the ruble's real value at roughly 2¢ rather than the official exchange rate of \$1.70—a freely convertible ruble is the *sine qua non* for true Soviet economic reform.

Setting a realistic value for the ruble would be a tremendous help to investors interested in the Soviet market. No longer would they be bewildered by the Alice-in-Wonderland maze of meaningless values for goods, farmlands, or factories that they might buy. It would also put pressure on the Soviets to phase out controls and let prices seek a realistic level throughout their economy.

Admittedly, the scheme has major problems. It will surely fail if the Soviets don't follow through by introducing true market reforms, such as allowing individuals to own and trade property without bureaucratic interference. Assets are not just rubles, need real values. And a stabilization fund requires big money, as much as \$15 billion or \$20 billion in a world in which capital is in short supply. Despite these impediments, however, the prospect of a ruble-stabilization fund is the most innovative idea to come out of London.

August 5

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THE STRATEGY BEHIND PHILIPS' DEAL WITH D

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BusinessWeek

AUGUST 5, 1991

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ARE YOU REALLY INSURED?

► Is Your
Pension
Money
At
Risk?

► What
About
That
Policy
You
Bought?

► Just
How
Bad Will
This
Get?

► What
You Can
Do To
Protect
Yourself

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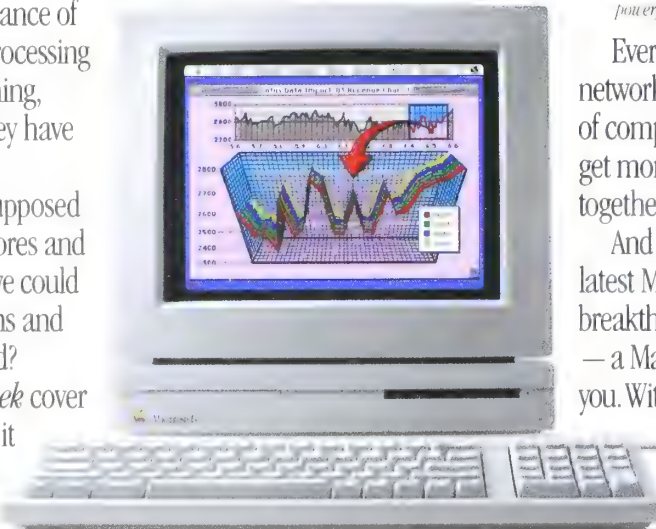
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System 7 for Macintosh. 



THE INSURANCE INDUSTRY HAS
LOST ITS ROCK-SOLID IMAGE

Money Story

42 ARE YOU REALLY INSURED?

The surety life policy is a contract that lets you borrow from the surety for cash or benefits. And now, as other policyholders want to know if they can borrow too, the surety industry is in a bit of a bind. The answer? Yes. But you'll have to do plenty of homework. To help, *BusinessWeek* has assembled a guide to the surety industry.

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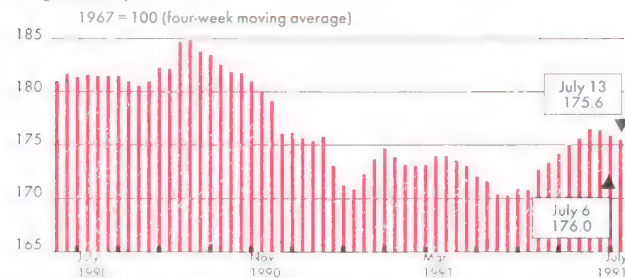
Hold the same stick over all insurers
The playing field is level—so play

BusinessWeek Index

PRODUCTION

Change from last week: -0.2%

Change from last year: -3.4%



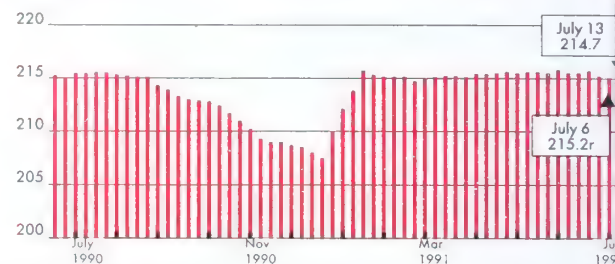
The production index dropped during the week of July 13. On a seasonally adjusted basis, truck production was cut by one-fifth, and output levels of electric power, crude-oil refining, steel, paper, and paperboard were all down as well. Rail-freight traffic, and coal, lumber, and auto production increased strongly. Before calculation of the four-week moving average, the index advanced to 176.5, from 172.6 in the previous week.

BW production index copyright 1991 by McGraw-Hill Inc.

LEADING

Change from last week: -0.2%

Change from last year: -0.4%



The leading index decreased modestly during the week ended July 13. The index has moved little so far this year, suggesting a very slow recovery. A sharp decline in materials prices, and slower growth rates for M2 and real estate loans offset the positive signs of higher stock prices and a drop in the number of business failures. Yields on long-term bonds were unchanged. Before calculation of the four-week moving average, the index fell to 213.7, from 214.3 in the week before.

Leading index copyright 1991 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (7/20) thous. of net tons	1,600	1,599#	-13.2
AUTOS (7/20) units	97,797	84,158r#	8.1
TRUCKS (7/20) units	71,135	38,792r#	-2.1
ELECTRIC POWER (7/20) millions of kilowatt-hours	66,980	64,778#	7.1
CRUDE-OIL REFINING (7/20) thous. of bbl./day	13,798	13,429#	-3.5
COAL (7/13) thous. of net tons	18,042#	13,574	-3.8
PAPERBOARD (7/13) thous. of tons	740.7#	747.8r	2.1
PAPER (7/13) thous. of tons	674.0#	717.0r	-7.8
LUMBER (7/13) millions of ft.	503.2#	341.1	13.6
RAIL FREIGHT (7/13) billions of ton-miles	18.7#	15.3	-5.6

Sources: American Iron & Steel Inst., Ward's Automotive Reports, Edison Electric Inst., American Petroleum Inst., Energy Dept., American Paper Inst., WWPA, SFPA, Association of American Railroads

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (7/24)	137	137	1.51
GERMAN MARK (7/24)	1.73	1.79	1.62
BRITISH POUND (7/24)	1.70	1.65	1.82
FRENCH FRANC (7/24)	5.89	6.08	5.44
CANADIAN DOLLAR (7/24)	1.15	1.15	1.15
SWISS FRANC (7/24)	1.51	1.55	1.38
MEXICAN PESO (7/24)	3,017	3,016	2,876

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound expressed in dollars.

PRICES

	Latest week	Week ago	% Change year ago
GOLD (7/24) \$/troy oz.	366.000	368.900	-1.8
STEEL SCRAP (7/23) #1 heavy, \$/ton	89.00	89.00	-19.5
FOODSTUFFS (7/22) index, 1967=100	198.7	197.0	-11.1
COPPER (7/20) ¢/lb.	103.2	104.6	-18.7
ALUMINUM (7/20) ¢/lb.	60.0	60.3	-17.8
WHEAT (7/20) #2 hard, \$/bu.	2.86	2.80	-7.1
COTTON (7/20) strict low middling 1-1/16 in., ¢/lb.	70.91	72.53	-11.3

Sources: London Wed. final setting, Chicago mkt., Commodity Research Bureau, Metals Week Kansas City mkt., Memphis mkt.

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (7/19) S&P 500	382.95	377.40	4.0
CORPORATE BOND YIELD, Aaa (7/19)	8.99%	9.04%	-2.0
INDUSTRIAL MATERIALS PRICES (7/19)	97.8	98.4	-3.0
BUSINESS FAILURES (7/12)	354	380	42.0
REAL ESTATE LOANS (7/10) billions	\$403.7	\$403.8	6.0
MONEY SUPPLY, M2 (7/8) billions	\$3,389.3	\$3,395.6r	3.0
INITIAL CLAIMS, UNEMPLOYMENT (7/6) thous.	395	388	9.0

Sources: Standard & Poors, Moodys, Journal of Commerce (index: 1980=100), Dun & Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. CIBCR seasonally adjusts data on business failures and real estate loans

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
ORDERS FOR DURABLE GOODS: MFG. (June) billions	\$116.5	\$118.4r	-8.0
HOUSING STARTS (June) annual rate, thous.	1,040	989r	-12.0
CONSUMER PRICE INDEX (June)	136.0	135.6	4.0
REAL GROSS WEEKLY PAY (June)	\$258.75	\$256.32	-1.0

Sources: Commerce Dept., BLS

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (7/8)	\$856.7	\$861.9r	5.0
BANKS' BUSINESS LOANS (7/10)	307.0	308.8r	-6.0
FREE RESERVES (7/10)	303r	979r	-39.0
NONFINANCIAL COMMERCIAL PAPER (7/10)	148.1	148.8r	0.0

Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed for two-week period in millions).

MONEY MARKET RATES

	Latest week	Week ago	% Change year ago
FEDERAL FUNDS (7/23)	5.74%	5.91%	8.05
PRIME (7/24)	8.50	8.50	10.00
COMMERCIAL PAPER 3-MONTH (7/23)	6.00	6.03	7.88
CERTIFICATES OF DEPOSIT 3-MONTH (7/24)	5.94	5.97	7.98
EURODOLLAR 3-MONTH (7/20)	6.00	6.06	8.05

Sources: Federal Reserve Board, First Boston

#Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

BOMBAY SAPPHIRE. POUR SOMETHING PRICELESS.



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AFFIRMATIVE ACTION: A GREAT LEVELER—OR DESTROYER?

I believe that you greatly underestimate the backlash against affirmative action that is building in this country ("Race in the workplace," Cover Story, July 8).

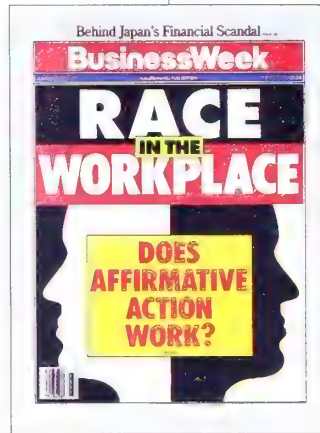
Lowered college-en-
trance requirements,
“race-norming” of em-
ployment-test scores, and
race- and gender-based
hiring and promotion are
widely and increasingly
resented by the white
population. You did not
cover federal agencies,
which have established
time goals for quotas
that may preclude the
hiring—and may even re-
quire firing—of white
males until the quotas
are met. They have also
discarded skill requirements, so that per-
sons without applicable training or expe-
rience can be placed in management po-
sitions over trained and experienced
white males.

No reasonable person would begrudge a job or promotion fairly earned, but consistently cheating deserving people in the name of civil rights can only result in race hatred. Racial justice and harmony can be achieved only by evaluating each person objectively on his or her merits.

Karl F. Wenger
Burgess, Va.

It is extremely uplifting and heartening to see a business publication offer an objective assessment of affirmative-action policies, and, more surprisingly, advocate their continuance. The rhetoric of both the right and the left is extreme, inflammatory, and accomplishes nothing other than continued polarization. It is painfully obvious to me, working in Corporate America, that racism and discrimination still cut across ethnic, religious, and gender lines. The playing field is not yet level.

Dave Tayeh
Chicago



Recently, I was prevented from promoting a minority woman by the affirmative-action policies of the organization for which I work. These policies required that all positions be advertised and that no internal candidate be considered unless she or he had formally applied for the position.

Today, job seekers are urged to network, but the usual networks are not readily available to many minorities. Renewed emphasis needs to be placed on promotion of qualified minority employees. And as your article points out, much more needs to be done in and out of the workplace to reduce the inaccurate perceptions that affect managerial evaluation of minority employees and often affect actual performance. Affirmative action, with its focus on statistics and procedures, may not be as helpful as it once was in attaining these goals.

Carole A. Aldrich
Durham, N. H.

Colton Isadore, a black maintenance supervisor at Monsanto's Chocolate Bayou chemical complex in southeast Texas, was quoted as saying: "We don't want quotas, and we don't need quotas." He continued to explain that the white backlash would really set things back. It is ironic, and comical in a sense, to read such comments from a black working in the post-segregationist South. A sophisticated black would quickly realize that if African-Americans such as Malcolm X, Martin Luther King, Medgar Evers, and others had taken the position that Afri-

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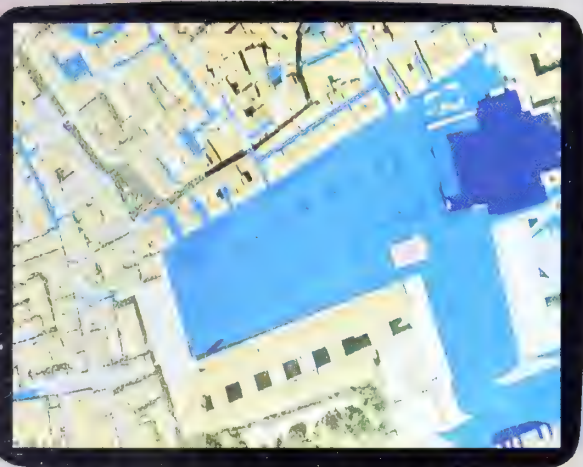
BUSINESS WEEK
AUGUST 5, 1991 ***3225
ISSN 0007-7135

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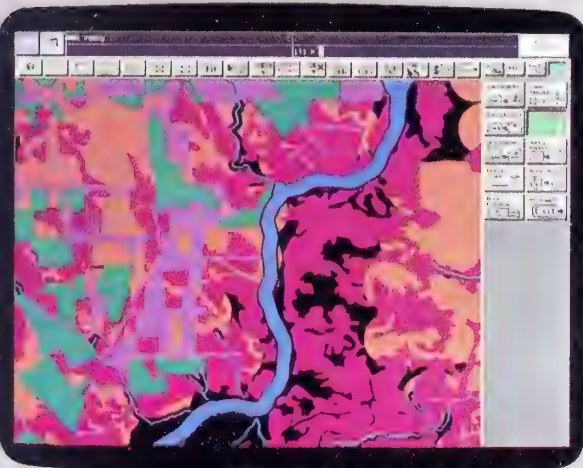
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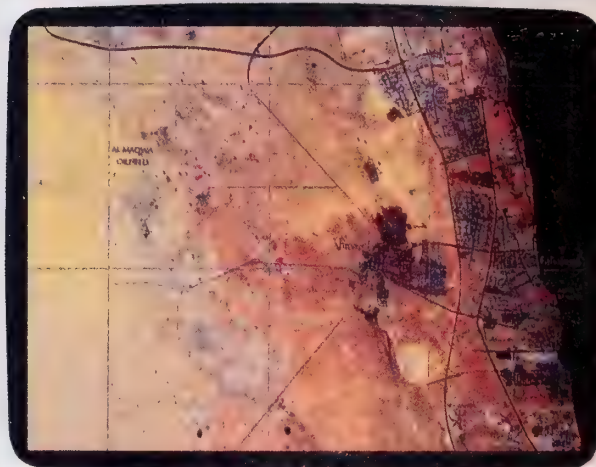
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Readers Report

can-Americans' rights weren't needed and should not be fought for, Jim Crow laws would have prevailed, and meaningful employment for African-Americans in the South would have remained an impossibility.

B. A. Ellis Jr.
Philadelphia

American managers, regardless of gender, want to work with the tools, strategies, and people that allow them to feel comfortable. Exceed your boss's threshold of discomfort, and you risk your career. Unfortunately, sometimes just being black puts you over that threshold.

Few CEOs seem to recognize that innovation and action require a certain level of discomfort and tension. It is all too rare to find a CEO who will demand that employees live with a higher degree of discomfort, see the chaotic ethnic world around them as it really is, and develop innovative solutions. Yet somehow American CEOs expect to succeed globally in diverse world markets when they have failed to handle ethnic diversity well at home.

Ted Allen
Silver Spring, Md.

Your story says that only 10% of whites report they have been victims of reverse discrimination. If we can assume white women would not make that assertion, we may find as many as 20% of white men aggrieved. According to the box on the same page, 44% of the work force would be white males, so "only" about 9% of the labor force feels victimized—or close to the proportion of the work force that is black.

Your conclusion seems to be that if 10 million or 11 million white men are discomfited, it is not important. It might be well to reflect that most of these men and their families vote and that George Bush swept the country with a majority of 7 million votes in 1988.

Stanley E. Honig
Lancaster, Pa.

Your stand in favor of affirmative action is proof that big business is every bit as great an enemy to freedom as is big government.

Larry Warner
San Diego

Perhaps this is your way of meeting a quota of minority-oriented articles. The entire problems of minorities can be summed up in three words: education, education, education. But that puts the burden of example and supervision on the father and mother, the school, the police, the civic leaders, and

the religious leaders of the community. But it's so much easier for minorities to blame someone else for their problems. Educated people of all races do not need to have affirmative action or quotas. They qualify for jobs and are productive citizens—no one can take their jobs away. It has been a long time coming, but now it's time to start telling it the way it really is.

John Anagnos
Wethersfield, Conn.

As a human-relations (HR) manager for a Massachusetts manufacturer, I was especially interested in your cover story. Of the 404 senior executives interviewed for the BUSINESS WEEK/Harris Poll, how many were actually in a position to know just how much effort their HR group expends to comply with affirmative action and Equal Employment Opportunity Commission regulations? I'll bet over half of the 53% responding "not much trouble" have no idea of the time and money spent in developing and implementing a plan (recruiting, tracking, training, etc.) nor could many articulate the penalties for noncompliance. Please pass the Excedrin for executive-order headache No. 11,246!

Karen S. Mehegan
Acton, Mass.

I must take the time to thank you for your story. I am a recent black graduate in engineering of predominantly black North Carolina Agricultural & Technical State University. Many of my fellow graduates expressed pessimism about being given a fair chance to enter or advance in the predominantly white workplace. I have preached for some time that we will be given the opportunity to prove ourselves, because the movement of American business to a world economy forces the development of all untapped and underused human resources.

I think your article clearly indicates that affirmative action in the workplace will stand firm despite the strikes against it by the Supreme Court and the White House. The evidence is in the faces seen at the marketplace and in the numbers seen on the balance sheet.

Cedric A. Dobson
Corning, N. Y.

Hordes of middle-class lawyers, politicians, "diversity managers," editors, and executives are striking "politically correct" poses, and they are passing on the cost to another group: poor whites.

This achievement of saintliness on the cheap is a blatant example of social and

political cynicism. By failing to deal with the very real concerns of the group, presently paying the highest price for a native action, you encourage and report this exploitation of the political helpless.

Your article failed even to mention, alone assess, the cost of affirmative action to this most highly affected group. Ignoring this facet of the issue perpetuates a real and growing injustice.

Thomas J. Riel
Knoxville, Tenn.

I read nothing about work quality or job performance when hiring or promoting. The minute you put a person's skin color or gender at the top of the list and job performance second, you gate the quality of the work that needed and create morale problems in the workplace.

I believe that affirmative action for minorities can and does work against them. Well-qualified minority candidates (and there are a lot of them) who are promoted may never get the respect they deserve from their peers who may see the promotion as a symbol of tokenism, not the result of good work.

I am not against helping minorities achieve job status, but let's give them a hand, not a hand-out.

Daniel J. Mahoney
Concord, Cal.

The question is not whether affirmative action works but whether affirmative action is right.

If it is wrong to discriminate against certain individuals solely on the basis of race, sex, or ethnicity, then it is equally wrong to discriminate in favor of such individuals solely on the basis of race, sex, or ethnicity.

Two wrongs still do not make a right.

Donald E. Horace
Agoura, Calif.

'Managing Diversity' is not a "politically well-scrubbed name for policies aimed at bringing minorities into the business mainstream through preferential hiring and promotion." Rather, it is creating an environment where everyone, including employees who are nontraditional (not white males) can fully contribute, are motivated, and have the opportunity to move into top management.

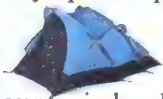
Iris Randall
New York

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BANKRUPT: RESTORING THE HEALTH AND PROFITABILITY OF OUR BANKING SYSTEM

By Lowell L. Bryan
HarperBusiness • 315pp • \$22.95

WHAT'S TO BECOME OF OUR BANKS?

Every day, it seems, we are bombarded by bad news from the world of banking. Even as Congress tries to fashion reforms to cure the industry's ills, one banking giant after another agrees to merge with a rival, declares huge losses, or otherwise teeters toward insolvency. Meanwhile, taxpayers are wondering whether they'll get stuck paying to clean up the banks—the way they must pay to restructure the savings and loan industry.

For those who yearn for a systematic understanding of this crisis, two experts—Lowell L. Bryan, a director at McKinsey & Co., and James L. Pierce, an economics professor at the University of California at Berkeley—have written books to provide just that. Of the two, Pierce's *The Future of Banking* is briefer and easier to follow. It takes a historical approach, while Bryan's *Bankrupt* follows the more abstract lines of economic analysis. Yet Bryan offers fresher, more profound thinking about solving the industry's problems. Indeed, his chief proposal—to break banks up into relatively safe, federally insured units and riskier, uninsured units—is gaining currency among lawmakers.

In exploring the roots of the crisis, Bryan and Pierce both acknowledge the tension that arises from banks' role as private businesses with a public purpose. While banks are profitmaking enterprises, they also have a duty to provide a safe haven for deposits and thus ensure some stability in the financial system. Throughout the industry's history, the two roles have vied for supremacy.

Both authors trace the banking system's current weakness to reforms enacted after the massive bank failures of the Depression. The regulatory framework established then effectively ended bank panics, which had long plagued the system. The new rules included federal deposit insurance, the separation of banking from other financial businesses, and such efforts to limit competition as ceilings on interest paid on deposits and restrictions on interstate branching. For more than three decades the reforms worked, protecting the public and guaranteeing profits for the banks.

But by the mid-1960s, Pierce writes, inflation and technological changes undermined the arrangement. When re-

THE FUTURE OF BANKING

By James L. Pierce
Yale University Press • 163pp • \$25

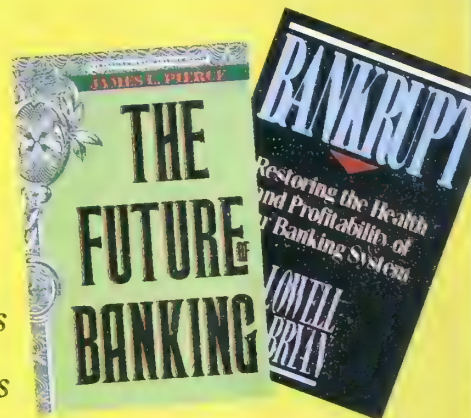
strictive monetary policy drove interest rates up, depositors left banks for higher-yielding, unregulated money-market accounts. But after Congress finally deregulated bank deposit rates in the early 1980s, high interest rates and recession squeezed profits.

Meanwhile, companies that would normally use banks were turning to the securities markets. At the same time, computers began to enable banks to raise deposits around the world. Flush with deposits but prohibited from venturing beyond the loan business, banks

such as Treasuries and mortgage-backed securities. Bryan contends that, despite their mundane business, core banks could attain a healthy return on assets of more than 1%, since deposit rates would be low and returns would not be eaten up by losses on risky loans. (In a brief final chapter, Pierce endorses a similar remedy. Under his plan, the insured entities could not make loans.)

Bryan envisions 10 to 20 large, metropolitan regional core banks with assets of \$100 billion to \$200 billion or more operating from such centers as Detroit, San Francisco, and Charlotte, N.C. They would be formed through mergers of what are now the 120 biggest bank holding companies, with two-thirds of the nation's deposits. Of the \$2.6 trillion now in bank deposits, Bryan calculates, about \$1 billion might leave core banks for higher yields offered elsewhere. Ultimately, he envisions thousands of small, independent core banks across the country.

One way to clean up the mess: Create insured 'core banks' that only take deposits and make small loans



sought better returns through high-risk lending—including loans to the Third World and commercial real estate. They suffered humiliating losses.

Bryan's solution is a fundamental change in the structure of banking. He would separate banks' business lines into three new entities. The safe businesses of taking deposits and lending to small enterprises would be carried out by federally insured "core banks." More hazardous businesses would be the province of two types of uninsured entities—money-market investment banks to engage in investment-banking activities and finance companies to make loans for real estate and other risky activities.

Core banks would pay Treasury rates on deposits, and the size of the loans they make would be limited. Since deposits probably would exceed the demand for small business loans, they could invest the excess in AA-rated securities,

a handful of large money-market investment banks and finance companies.

Although Bryan's vision is radical, lawmakers seem increasingly intrigued by the idea. Representative Charles Schumer (D-N.Y.) plans to introduce the core bank concept in an amendment pending legislation when it comes to House vote. For now, however, Congress is more likely to settle for dismantling some Depression-era regulations.

Together, Pierce, with his discussion of the origins of the banking crisis, and Bryan, with his proposal for a way out, provide a primer on a subject that deserves urgent attention. Notes Bryan: "As a nation, we only have one banking system and one economy.... If we try to muddle through this mess, we will suffer collectively."

BY CATHERINE YAN

Washington Correspondent Yang covers banks and savings and loans.

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The Energy To Change



IF THIS IS RECOVERY, KISS THE KEYNESIANS GOOD-BYE

BY PAUL CRAIG ROBERTS



For the recession to end without government intervention would mean there's no truth in the economic doctrine that has guided economic policy in the postwar period

Whither the economy? A weak recovery, a strong recovery, or a double-dip recession? Forecasters differ in how they read the tea leaves. In thinking about how to place your bets, consider the following:

If there is a recovery, weak or strong, it will be the first in the post-World War II era that is not led by government policy. There is no monetary expansion to get the economy going, and Washington isn't providing any fiscal stimulus. To the contrary, the recovery will have to occur despite what Federal Reserve Board Chairman Alan Greenspan calls the continuing credit crunch and higher taxes at federal, state, and local levels.

It would be a blow to Keynesians if recovery happens in the face of what they regard as policies that reinforce the business cycle. That would mean there is not a single truth in the economic doctrine that guided postwar policy. If placing John Maynard Keynes and his followers—who have garnered most of the Nobel prizes in economics—in the same category with Karl Marx is an implausible thought, then so is the forecast of recovery.

The leading principle of the Keynesian revolution is that market economies are not self-correcting. Without fiscal and monetary stimulus, unemployment feeds on itself as falling incomes limit demand, leading to a downward spiral. The economy would come to equilibrium at less than full employment and active anti-cyclical policies would be necessary to keep the economy from becoming stuck below its full potential.

A budget deficit and lower interest rates because of weak demand don't qualify as active antirecessionary policies. To be stimulative, the deficit must increase. Also, it must be a discretionary increase by policymakers over and above the rise in red ink from built-in stabilizers (lower tax receipts and rising unemployment and welfare payments) that automatically operate in a recession. Textbooks continue to stress "that built-in stabilizers are a first line of defense but are not by themselves sufficient to maintain full stability" (Paul A. Samuelson, *Economics*, 12th ed.).

NO RESERVE. Looking at our current economy, the Keynesians who taught me would be worrying about parallels to the mistakes that contributed to the distress of the 1930s. They would point out that many investors and financial institutions made long-term commitments with the expectation that policies of high demand would continue, only to find themselves undercut by government policy.

Expecting tax cuts and \$200 billion budget deficits as far as the eye can see to sustain in-

flation, investors flocked into real estate seeking an inflation hedge with a proven track record. Banks lent readily, relying on rising real estate values as collateral, and they failed to reserve against their massive Third World loans, counting on inflation to bail them out by raising oil and commodity prices.

No one expected inflation to collapse, much less remain low during a lengthy economic expansion. As miscalculations came home to roost, the government pulled the tax rug out from under real estate investments with the 1986 tax-reform bill. As prices fell and investors fled, the value of the collateral behind thrift and bank loans shrank, eating up the capital of the lending institutions.

As troubles mounted, the government destroyed the value of savings and loan charters with the ill-considered 1989 S&L legislation. My Keynesian teachers would have described that as an act of madness certain to contribute to the downward spiral and to spread the problem into other financial institutions. Not that commercial banks have found their capital positions under pressure, the government has responded by proposing, during a recession, banking legislation that encourages bankers to build their capital ratios by not lending.

LOSING FAITH? A Keynesian analysis of these events would find a prescription for "debt deflation." *The New York Times'* front-page headline of July 5, "Bankers expected to stay hesitant to lend for years," together with attendant cutbacks in state budgets, would not foretell a recovery to a Keynesian economist.

If the economy recovers from recession despite procyclical policies, it will discredit Keynesian economics. The maligned and caricatured classical economists, who believed in laissez-faire and Say's law (supply creates its own demand), will have triumphed over the postwar generation of interventionist economists, who stressed demand management to offset the "deflationary gap" that is still illustrated in economics textbooks.

Before letting hopes for recovery succumb to the authority of postwar economics, consider that economists themselves have lost faith. This recession did not produce the usual calls for countercyclical measures to restore full employment. Instead, economists cautioned against disturbing the recently enacted budget agreement designed to shrink the deficit and advised that the economy would be on the upswing before government could implement an antirecessionary policy. If this overthrow of Keynesian prescriptions proves to be a mistake, President Bush's 1992 reelection hopes will disappear into the deflationary gap.

PAUL CRAIG ROBERTS IS CHAIRMAN OF THE INSTITUTE FOR POLITICAL ECONOMY IN WASHINGTON

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BY MICHAEL J. MANDEL

THE SLUMP STRUCK SOME STATES MORE THAN ONCE

If the recession of 1990-91 is a puzzle for economists, in part that's because two different recessions have been rolled into one.

On the one hand, a deep downturn in manufacturing has cost some 680,000 jobs over the past year, but the pain has been spread out evenly across the country. Based on the most recent figures from the Bureau of Labor Statistics, 41 states saw a decline in manufacturing employment in the year from

such states as Texas and Washington, even during the recession. In the five states that showed the greatest job gains over the past year, nearly 90% of the growth came from the service sector (chart). One example: The oil shock helped Texas gain some 6,000 oil-related jobs in the past year, but 32,000 new government jobs were much more important in helping the state grow.

The apparent vigor of the service sector outside of New York, Massachusetts, and New Jersey means that as the manufacturing sector revs up again, most parts of the country will see a real economic expansion. But the depth of the service-sector downturn in these three states underscores the struggle they face to get back to economic health.

study by C. Alan Garner, a senior economist at the Federal Reserve Bank of Kansas City, consumer-confidence measures usually don't accurately forecast consumer spending. Toward the end of the 1981-82 recession, a drop in consumer confidence gave few clues that a sustained recovery in durable-goods purchases, such as cars, was about to begin. And measures of confidence stood at an all-time high in 1989, even as consumers were starting to cut back.

Garner suggests that watching consumer confidence makes sense only during exceptional events, such as war, when consumer sentiment can rapidly shift. But once the war is over, paying too close attention to confidence measures can be a mistake. Since March, the Conference Board's Index of Consumer Confidence has drifted downward 4%. If Garner's analysis is right, though, that needn't rule out a continued improvement in consumer spending.

SAVINGS WON'T BE GETTING A BOOST FROM BOOMERS

With a savings rate well under 5% in recent years, the U.S. has lost its global reputation as a nation of spendthrifts. Some economists have optimistically suggested that this may soon change as an aging baby-boomer population starts putting away money to cover college costs and retirement. But a new report by economist Edward McKelvey of Goldman, Sachs & Co. says much more downside, arguing that demographic changes are likely to provide only a scant increase in savings. First, says McKelvey, "there's little evidence that excessive consumption by yuppies is responsible for the saving slump." True, consumers did save less. But McKelvey calculates that they were spending more on medical care rather than splurging on such discretionary purchases as clothing and recreation. As the boomers age, medical expenses are likely to rise rather than fall.

McKelvey also points out that baby boomers just aren't numerous enough to boost the savings rate very much. To be sure, households headed by 45- to 54-year-olds save some 8.1% of their income, about twice the national average. And this group will make up 20.2% of the population by the year 2000, up from 15.5% in 1990. But this shift would increase the savings rate by only half a percentage point—far less than some have predicted. So according to McKelvey's analysis, the savings rate will get no free ride from demographics.

THE RECESSION'S UNEVEN TOLL

JOB LOSERS

Change in payroll employment* / Thousands

NEW YORK	-160.8
MASSACHUSETTS	-152.5
MICHIGAN	-93.0
NEW JERSEY	-80.9
PENNSYLVANIA	-39.0

JOB GAINERS

TEXAS	83.7
WASHINGTON	47.9
COLORADO	34.0
NEBRASKA	33.2
LOUISIANA	30.5

*From April-May, 1990, to April-May, 1991

DATA: BUREAU OF LABOR STATISTICS

April-May, 1990, to April-May, 1991. The biggest loser was California, with a fall of 86,000 manufacturing jobs, but there were 10 other states where the manufacturing-employment loss exceeded 20,000.

By contrast, the recession in the service sector—ranging from banking to retailing to government—has zeroed in on just three states: New York, Massachusetts, and New Jersey. The U.S. overall lost about 40,000 finance jobs in the past year. However, that decline was concentrated in those three states, which are account for 94% of the decline in financial-sector employment. The same three laggards are responsible for 76% of the drop in U.S. retail and wholesaler trade jobs. And while New York, Massachusetts, and New Jersey were losing some 53,000 federal, state, and local government jobs, the rest of the country was adding 129,000 government jobs.

The service sector has expanded in

GOOD NEWS (SORT OF) FOR DEFICIT-BURDENED TAXPAYERS

Worries about the record 1992 budget deficit—now estimated to hit \$348 billion—have helped keep long-term interest rates up around 8.5%. But the deficit may be much easier to finance than expected, suggests economist Maury Harris of PaineWebber Inc. His reason: More than half of the deficit is the result of interest payments on the national debt, and much of the rest consists of payoffs on bank deposit insurance. And these types of outlays, unlike government purchases of goods and services, are available to be lent back to the government again. For example, most interest payments go to institutions and high-income individuals who reinvest the money rather than spend it. So even the big deficit, says Harris, won't stop long-term interest rates from falling to 7.5% by mid-1992.

A CONFIDENCE CRISIS IN CONSUMER-CONFIDENCE FORECASTS?

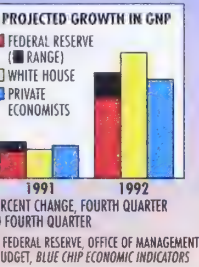
The Conference Board and the University of Michigan have published their measures of consumer confidence for years, but they hit the big time during the Persian Gulf war. When consumer confidence dropped almost 40% after Iraq's invasion of Kuwait last August, economists forecast that consumers were going to spend less. And the rebound of confidence in March, 1991, was seen as a sign that consumers were ready to buy cars and homes again. But the recovery may be fleeting for these indicators. According to an upcoming

LOWER INTEREST RATES? THE PRICE MAY BE A WEAK RECOVERY

Forecasting interest rates is a lot different from predicting gross national product. Economists stand to lose more than their credibility. They can lose someone's money.

Right now, the outlook for interest rates is especially bleak. No one has a clue about what the Federal Reserve's next move on short-term rates will be. Worries in the bond market about inflation and the huge borrowing needs of the Treasury Dept. are clouding the outlook for long-term rates. And on top of it all, the recovery has yet revealed its true identity: Will it be Arnold Schwarzenegger or Pee Wee Herman?

DIFFERING VIEWS ON THE ECONOMY



To be sure, the Bush Administration would like the economy to show some muscle as it heads into the 1992 election year dragging along a \$350 billion budget deficit. But the Fed and the bond market are more comfortable with the consensus forecast of a relatively meek recovery (chart). Given their power to influence the outcome, the central bank and bond traders

are more likely to get their wish.

If that's true, the Fed will be able to hold short rates relatively steady during the second half. The rate on three-month Treasury bills, for example, has held close to 5.6% since early June. And long-term rates should remain in the range they have occupied for most of the year, 8.25% to 8.75%, as the improving outlook for inflation offsets the Treasury-led flood of new borrowing.

THE FED IS SETTLING ON LOWER INFLATION

Alan Greenspan's remarks to Congress on July 16, the chances for additional easing in coming months are greater than those for a new round of tightening. Greenspan's glowing prospects for inflation seem to include the need for higher short-term interest rates, as long as the recovery isn't overly strong. The central bank looks for consumer prices to rise in the range of 3% to 3.75% this year and 3% to 4% in 1992.

Moreover, Greenspan suggested that the squeeze on credit creation in the banking system, along with the cure of money growth to pick up, is a genuine risk to the recovery. He seemed to leave the door open to lower rates if the upturn shows signs of faltering.

Sluggish growth in money and credit is attracting increasing concern from both Washington and Wall Street. Top White House economist Michael J. Boskin calls the problem of credit availability "the single biggest threat to a sustained recovery." Many private economists question the upturn's viability in the face of unusually weak money growth. And even Fed officials admit to surprise over the latest money numbers.

M2, the most closely watched money measure, fell a sharp \$6.9 billion in early July. M2 is now growing at an annual rate of only 3.1% from the fourth quarter of 1990, well below the midpoint of the Fed's 2.5%-to-6.5% target range (chart). During the first two quarters of the past five recoveries, M2 has grown somewhere between 8% and 16%, at an annual rate.



Some economists believe that money growth moves the economy, and some think that it is simply a reflection of business activity, but either way, the latest numbers do not bode well for an economy that is, according to most analysts, now three months into a recovery.

A lot depends on the rate at which money turns over, or velocity. As money turns over faster, a given pace of M2 can support greater growth in the dollar value of GNP. However, during the first year of the past five recoveries, M2 velocity has grown appreciably in only one case—and that was the short-lived recovery in 1980.

Without a pickup in either money growth or velocity, the current pace of M2 is inconsistent with the Fed's own forecast of 3% economic growth in the second half of 1991 and 2.25% to 3% in 1992. Amid sluggish money growth, the Fed will not lift short-term interest rates. Indeed, another cut in the federal funds rate, from 5.75% currently, seems likely by autumn.

HIGH LONG RATES MAY HURT THE RECOVERY

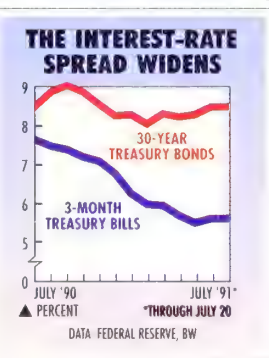
Forecasting long-term interest rates is no piece of cake, either. In some ways, long rates are more important to the economy than short rates. They influence the credit-sensitive demand for houses, cars, and other items that help give the business cycle its swing. And long rates are largely outside the Fed's control.

For now, the bond market is a little leery of Greenspan's bright inflation outlook. But even a slightly less sanguine view of future price growth, combined with the expectation of modest economic growth, makes a strong

Business Outlook

case that the yield on 30-year Treasury bonds, for example, should be well below its current level of about 8.5%.

The problem is a relentless supply of new Treasury issues, expected to hit the market this quarter at a clip of about \$1 billion a day. This is clogging the markets and keeping yields higher than they would otherwise be, particularly in relation to short-term rates (chart). In past recoveries, the yield spread typically widens, but it does so because short rates are falling faster than long rates, not because long rates are rising.



The failure of long rates to decline as they have in past recessions may be starting to hurt the recovery. Production of durable goods, where long rates play a crucial role, has been a leader in this upturn. However, new orders received by manufacturers of durable goods fell 1.6% in June, and after revision, the May gain was much less than originally reported (chart).

The housing recovery is also at risk. A July survey by the National Association of Home Builders noted a second consecutive month of erosion in home-buyer traffic, current sales, and builders' expectation of future sales.

THE WHITE HOUSE AND THE FED ARE AT ODDS

There is no hope for any break in Washington's borrowing needs. The federal budget deficit narrowed to \$2.5 billion in June, much less than the \$11.1 billion gap in June, 1990. However, a calendar quirk, which depressed outlays, and delays in the bailout of failed savings and loans caused the shrinkage.

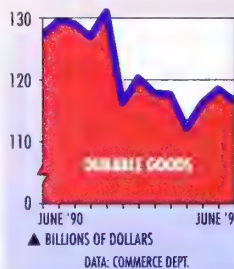
The White House estimates that the budget deficit is swelling to \$282 billion in the 1991 fiscal year, which ends in September, from \$220.1 billion in 1990. The Administration expects the gap in 1992 to balloon to \$348

billion, as the costs of the S&L bailout continue to mount.

For the near term, such pressures on the credit markets will keep long-term interest rates higher than other fundamentals would allow. The deficit will jump to about 5.8% of GNP in 1992. That's only a shade below the record of 6.3% hit in 1983, which resulted in high real interest rates that substantially crowded out private investment and stifled productivity growth. Such a scenario seems likely in the early 1990s as well.

Moreover, if the Administration does not get its projected 3.6% in economic growth next year, the deficit could top \$350 billion. Indeed, the Fed's goals for the economy are clearly at odds with those of the White House. Given the central bank's ability to influence the economy, its forecast of 2.25% to 3% for real GNP in 1992 looks like the upper limit on economic growth that the Fed feels is consistent with achieving its inflation goals.

NEW ORDERS DON'T SHOW MUCH BOUNCE



The improving outlook for inflation should vent some of the upward pressure on long rates. Price increases always slow in the early stages of an economic recovery, reflecting the time lags required to eliminate excess capacity in the markets for goods, services, and labor.

Add to that the Fed's preferences for slower price growth, and the bond market's inflation fears seem way out of line with reality. All this means that long-term rates will eventually decline from their current levels, but that might not happen until 1992.

Until then, what's shaping up is a battle between the Fed's objectives for inflation and the Administration's needs for economic growth. Clearly, lower long-term rates would please the White House as the Presidential campaign nears. But the irony is, it will probably have to lose its battle with the Fed in order to get them.

THE WEEK AHEAD

PERSONAL INCOME

Monday, July 29, 10 a.m.

Personal income likely rose by 0.5% in June, the same gain as in May, says a report by McGraw-Hill's MMS International. Consumer spending probably rose 0.4% in June, after jumping 1.1% in May.

EMPLOYMENT COSTS

Tuesday, July 30, 8:30 a.m.

Wage and benefit costs for private industry workers probably increased by about 1% in the second quarter. In the first quarter, they advanced by 1.1%.

NEW SINGLE-FAMILY HOME SALES

Tuesday, July 30, 10 a.m.

Sales of new homes are expected to rise

to an annual rate of 490,000 in June, from a 474,000 pace in May.

LEADING INDICATORS

Wednesday, July 31, 8:30 a.m.

The index of leading indicators probably increased a sharp 0.8% in June, the same jump as in May. If so, it would be the fifth monthly rise in a row.

FACTORY INVENTORIES

Wednesday, July 31, 10 a.m.

Factory inventories likely fell by 0.5% in June, after dropping 0.8% in May.

CONSTRUCTION SPENDING

Thursday, Aug. 1, 10 a.m.

Construction outlays likely were unchanged in June, according to the MMS

consensus. In May, they fell a steep 0.9%. Increased homebuilding in June offset weakness elsewhere.

NAPM SURVEY

Thursday, Aug. 1, 10 a.m.

The National Association of Purchasing Management's index of industrial activity is expected to rise to 52.3% in July, from 50.9% in June. The rise suggests that the factory sector is recovering.

EMPLOYMENT

Friday, Aug. 2, 8:30 a.m.

The MMS economists expect that non-farm payrolls added 70,000 workers in July, reversing the 50,000 loss of June. The jobless rate for July is projected to be unchanged from June's 7% level.



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AUGUST 5, 1991

THE END OF THE SLIDE?

PROFITS ARE COMING BACK. MODESTLY

The global economy can be a blessing, it can be a curse, and sometimes it can be both at once. Just look at corporate profits. Even though the recession didn't officially begin until the third quarter of 1990, earnings had been falling for more than a year before (chart), partly because of tough price competition from foreign companies. But after the U.S. economy slipped into recession, earnings of American companies held up fairly well because they got a boost from overseas.

Now, by most accounts, the U.S. economy is on the mend. But the rebound in corporate profits may be restrained. What's holding them back? You guessed it: Many overseas economies are slowing down, putting a drag on revenue gains. And tough foreign rivals aren't going to allow any leeway on pricing.

The mixed news from overseas complicates an already problematic second-quarter profit picture. The biggest uncertainty, of course, is the state of the economy. The recovery may have arrived, but you wouldn't know it from looking at second-quarter earnings reports. When the numbers are all in, they are expected to show a 9% decline from the second quarter of 1990. But the good news is that the latest results should mark the end of the slide in corporate earnings that started in the third quarter of 1989.

One caveat: It's possible that earnings for the third quarter may be flat or down slightly. But that's something of a statistical illusion. Last year's third quarter showed a surprising 10% gain over the third quarter of 1989.

That certainly wasn't typical of the year as a whole.

Moreover, the rising tide in the third quarter of 1991 won't lift every boat: Hard-hit sectors such as steel and computers will continue to report down earnings through the end of the year. But most economists figure that after the second quarter, the trend for corporate profits is up.

NO 'BIG PARTY'. It's not likely, though, that full-year earnings per share for the Standard & Poor's 500-stock index will rise much above their 1990 level. That's because the economy may not



Because steel trails economic turns by about six months, analysts don't think it will show a solid profit recovery until 1993

economist at 3M Co. thinks the trend toward just-in-time inventory has kept companies from placing big orders that would pump up the economy. "We're seeing lots of hand-to-mouth buying," he says. The result, says Susan Lakatos, a Kidder Peabody & Co. vice-president: "We won't get the big party that we normally have at the end of a recession." She expects S&P 500 earnings to rise only 11.6% next year.

Those numbers will be rising from a relatively low base. Even though the recession didn't officially begin until the third quarter of 1990, the sluggish growth that persisted for the year or so before that took its toll on profits. Weak demand and intense competition from foreign corporations made it tough for U.S. companies to raise prices at the same time that wages, benefits, and interest costs were on the rise. The result: Profit margins got squeezed.

bounce back as high as it usually does after a recession. In the average post-war business cycle, earnings for the S&P 500 have increased 23.9% in the year following a trough in real GNP, according to Rupert Thompson, an economist with UBS Phillips & Drew, a London-based securities firm. Thompson is projecting only a 17% increase in S&P 500 earnings during the first year of the latest recovery.

Ironically, the rebound may be hampered because Corporate America is getting smarter about the way it does business. John McDevitt, a corporate



Drugmakers came out with a host of new, high-margin products that allowed them to fare even better than usual in the latest downturn

in the second quarter (table).

While some companies had new products, others hauled out the pruning shears. Even before the recession was officially under way, companies were laying off workers and consolidating operations in anticipation of weaker demand. Roach says this strategy allowed companies to avoid the margin squeeze that usually occurs in a downturn. Indeed, Lakatos of Kidder Peabody says that aftertax operating profit margins rose from 6.3% in the fourth quarter of 1990 to 6.7% in the first quarter of 1991, when GNP fell at an annual rate of 2.8%. "The fact that profit margins began to stabilize despite a sharp downturn in GNP is persuasive evidence that recent cost-cutting and long-term restructuring are starting to pay off," says Lakatos.

FIGHTING TRIM. The chemical industry, for one, weathered this recession better than previous down cycles. Earnings per share of the companies in the S&P chemicals industry index declined 2.7% during the latest downturn (through the first quarter),

foreign competition may have kept prices on price increases, but the global economy also helped cushion the earnings of U.S. companies during the latest recession. In the typical postwar business cycle, earnings for the S&P declined 19.6%, says Thompson of Phillips & Drew. If this recession ended over, it will have been one of the mildest ones since World War II, Thompson estimates the drop in earnings will be 14.5% from the peak of GNP growth to the trough.

Earnings didn't drop more because U.S. companies got plenty of support from their foreign subsidiaries.

During the first two quarters of a downturn, the overseas component of U.S. corporate earnings usually falls about 5%, says Stephen Roach, senior economist with Morgan Stanley & Co. In the latest recession, the increase has been about 1%. "While some of this can be attributed to positive earnings translations of an undervalued currency," says Roach, "there can be no missing the role played by an

improvement in the nation's competitive position."

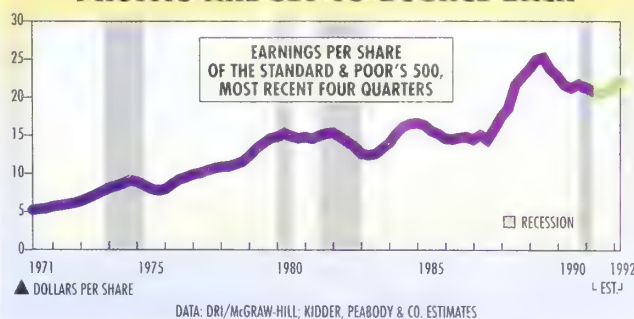
U.S. pharmaceuticals companies, in particular, are thriving in the global marketplace. Traditionally a recession-resistant industry, drugmakers came out with a host of high-margin new products that allowed them to fare even better than usual in the latest downturn. Companies in the S&P drug group posted a 16.9% gain in earnings, compared with a 9.6% increase in the 1974 down cycle. Baxter International, Bristol-Myers Squibb, and Merck all reported double-digit profit increases

compared with a 37% drop in the 1982 recession and a 38% decrease in the 1980 down cycle. The difference this time, says T. Kevin Swift, senior economist with the Chemical Manufacturers Assn. in Washington, is that by eliminating much of its excess capacity during the 1980s, the chemical industry minimized the impact of the recession. At Du Pont Co., for instance, U.S. employment—excluding its Conoco Inc. and Consolidation Coal Co. units—fell to 79,523 in 1991, from 105,171 in 1981. Now that it is in fighting trim, the company is poised for a spike in profits. Says a Du Pont spokesman: "With a turnup in the economy, we should see margins improve."

Moreover, says Swift, chemical production tends to be a leading indicator for the whole economy. So the upturn in chemical production in the past four months suggests that other areas of the economy will soon get moving again.

Not all sectors that purportedly got lean and mean during the 1980s had an easi-

AFTER A LONG SLIDE, PROFITS ARE SET TO BOUNCE BACK



AN EARLY LOOK AT SECOND-QUARTER PROFITS

The pluses, at last, are proliferating. Executives in the computer and capital-goods in-

dustries wouldn't say profits are recovering. But brokers and retailers have cause for hope.

	Sales \$ mil.	% chg. vs. 1990	Profits \$ mil.	% chg. vs. 1990	Margins	
					1991	1990
ABBOTT LABORATORIES	\$1,683.0	+12%	\$268.3	+12%	15.9%	16.0%
ALCOA	2,569.3	-5	81.2	-50	3.2	6.0
ADVANCED MICRO DEVICES	296.8	+11	17.3	NM	5.8	NM
AMERICAN CYANAMID	1,420.4	+16	131.8	+22	9.3	8.8
AMERICAN EXPRESS	6,363.0	+5	256.3	-20	4.0	5.3
AMERICAN HOME PRODUCTS	1,619.5	+1	265.2	-2	16.4	16.8
AMERITECH	2,742.1	+2	303.9	-14	11.1	13.1
AMHEUSER-BUSCH	3,260.8	+9	286.7	+11	8.8	8.6
BAXTER INTERNATIONAL	2,197.0	+10	141.0	+28	6.4	5.5
BELL ATLANTIC	3,081.4	0	355.1	-2	11.5	11.8
BLOCKBUSTER ENTERTAINMENT	210.1	+41	21.4	+44	10.2	10.0
BRISTOL-MYERS SQUIBB	2,730.4	+10	489.5	+17	17.9	16.8
CAPITAL CITIES/ABC	1,357.8	0	127.8	-10	9.4	10.5
CBS	709.4	-14	50.7	-63	7.1	16.7
COCA-COLA	3,039.5	+11	482.4	+18	15.9	15.0
COMPAQ COMPUTER	717.8	-17	20.3	-81	2.8	12.1
CONNER PERIPHERALS	405.4	+33	26.8	0	6.6	8.8
CORNING	778.2	+15	73.9	+10	9.5	9.9
CSX	2,125.0	+4	115.0	+6	5.4	5.3
CUMMINS ENGINE	877.6	+1	-17.2	NM	NM	0.7
DUPONT	10,031.0	+3	549.0	-21	5.5	7.1
EXXON	27,267.0	+5	1,125.0	+2	4.1	4.2
GENENTECH	117.6	+9	11.4	+114	9.7	4.9
GENERAL DYNAMICS	2,416.0	-8	211.0	NM	8.7	NM
GENERAL ELECTRIC	14,800.0	+3	1,131.0	+4	7.6	7.6
GEORGIA-PACIFIC	2,981.0	-15	33.0	-69	1.1	3.0
GTE	5,367.0	+1	403.0	0	7.5	7.6
HONEYWELL	1,520.2	-2	77.6	-16	5.1	6.0
IBM	14,732.0	-11	114.0	-92	0.8	8.5
INTEL	1,252.7	+29	230.8	+35	18.4	17.6
INTERNATIONAL PAPER	3,100.0	-4	104.0	-44	3.4	5.7
JOHNSON & JOHNSON	3,031.0	+8	406.0	+15	13.4	12.6
KROGER	5,086.4	+7	32.2	+28	0.6	0.5
LIZ CLAIBORNE	416.0	+22	39.5	+13	9.5	10.3
MARRIOTT	1,940.0	+10	27.0	-41	1.4	2.6
MAYTAG	777.6	-1	18.8	-38	2.4	3.9
MCDONALD'S	1,670.8	+1	232.0	+8	13.9	13.0
MCI COMMUNICATIONS	2,098.0	+12	137.0	-23	6.5	9.5
MERCK	2,122.4	+12	556.0	+18	26.2	24.8
MERRILL LYNCH	3,063.9	+7	184.3	+149	6.0	2.6
MOBIL	14,449.0	+5	445.0	-11	3.1	3.6
MORGAN STANLEY	1,627.5	+13	100.9	+74	6.2	4.0
MOTOROLA	2,814.0	+4	119.0	-26	4.2	5.9
NCR	1,556.0	-3	99.0	-14	6.4	7.2
PEPSICO	4,679.8	+11	318.3	+9	6.8	7.0
PHILIP MORRIS	14,770.0	+16	1,153.0	+22	7.8	7.4
RAYTHEON	2,357.0	0	151.8	+5	6.4	6.2
REEBOK INTERNATIONAL	688.3	+31	60.4	+39	8.8	8.2
REYNOLDS METALS	1,523.5	-1	61.4	-40	4.0	6.7
RJR NABISCO	3,780.0	+9	79.0	NM	2.1	NM
SAFEWAY	3,519.8	+2	35.6	+51	1.0	0.7
SCHLUMBERGER	1,552.7	+20	180.8	+25	11.6	11.2
SEARS, ROEBUCK	14,090.0	+2	239.3	+1	1.7	1.7
TEXACO	9,031.0	+4	269.0	-24	3.0	4.0
TRW	1,980.0	-6	24.0	-62	1.2	3.0
UNISYS	2,202.8	-11	-1,299.8	NM	NM	0.5
UNITED TECHNOLOGIES	5,376.9	-6	43.4	-79	0.8	3.6
WASTE MANAGEMENT	1,880.8	+34	206.9	+16	11.0	12.8
WESTINGHOUSE ELECTRIC	3,174.0	0	127.0	-50	4.0	7.9
WYERHAEUSER	2,296.6	-4	69.6	-39	3.0	4.8

NM not meaningful

DATA: STANDARD & POOR'S COMPUSTAT SERVICES INC.

er time in the latest recession. Though the big integrated steel producers such as USX and Bethlehem Steel Corp. have spent about \$14 billion over the past decade to modernize their factories, they have been unable to recoup that investment. Thanks to aggressive buying by powerful steel buyers in the auto and appliance industries, steel sells, on average, for the same price it did in the early 1980s. As a result, earnings per share for the S&P steel group plummeted 556.7% in the latest down cycle. By contrast, the group whose composition has changed over time, had an 237.8% drop in reported earnings during the 1982 recession and a 74.4% decline in the 1980 downturn.

Still, steel's restructuring has made the U.S. industry competitive with most foreign producers. And benefits from ongoing modernization should start to pay dividends when the economy works up a full head of steam. Because steel trails economic turns by about six months, analysts don't think there will be a solid steel profit recovery until 1993.

STRONGER GREENBACK. Most corporate earnings should get a lift from faster sales growth sooner than that, but they will lose some of the benefits from overseas earnings. A stronger dollar and slowing growth in foreign economies means that profits from overseas operations will flatten out and decline from their recent quarterly highs, says Richard D. Rippe, chief economist at Dean Witter Reynolds Inc. This trend is already apparent among technology companies such as Compaq Computer Corp., which reported an 81% decline in second-quarter profits. Ron Canio, Compaq's CEO, warns that weaker demand in Europe, severe price competition in the personal computer market and a strengthening greenback will hurt third-quarter earnings.

The overseas problems of the U.S. computer companies are further evidence that the world is a different place since the last recession. Tough competition from scrappy foreign players means that an expanding economy at home is no guarantee of rising profits. Conversely, strong demand at home is not enough to boost the earnings of many U.S. companies, which are more dependent than ever on foreign sales for growth. Whatever the drawbacks, though, more and more U.S. companies have little choice but to regard the whole world as the playing field.

By Monica Roman in New York, with Michael Schroeder in Pittsburgh, Joseph Weber in Philadelphia, Kevin Kelly in Chicago, and bureau reports

BUSINESS WON'T ANTE UP UNTIL GORBY NAMES THE GAME

tain investors' trust, he can't treat reform as just a possibility

When superpowers get together, nothing ever is certain. But the July 30-31 meeting in Moscow between President Bush and Soviet President Mikhail Gorbachev will be used as summits get to a sure thing. The signing of a historic arms-control deal as a centerpiece, the Moscow meeting is bound to be a political success for both leaders.

However, while Gorbachev and Bush enjoy photo ops from the Kremlin in Kiev, the pomp will obscure a sobering fact: For the U.S.-Soviet partnership in *perestroika* to succeed, reluctant Gorbachev has to stop talking economic reform as an intriguing theoretical possibility. "The White House says a senior White House official is to convince Gorbachev that he doesn't need to talk to the heads of government as much as he needs to convince Western investors that he is serious about business."

TO THE WEST. That's one tough sell. Would-be investors are waiting warily as the Soviet economy integrates. They're slow to put money down until they see whether Gorbachev can simultaneously handle pressure from reactionary hard-liners and negotiations with republics over the rules of the new government.

The London meeting of the Group of Seven industrial democracies added up the pressure on Gorbachev by taking away his excuses for continuing inaction on reform. The G-7 leaders decided on July 17 to give Moscow associate status in the International Monetary Fund and World Bank—and, along with that, access to a deep pool of expertise in the transformation of socialist economies. Washington officials believe that if Gorbachev is interested, the IMF can in a few months provide him with a detailed reform plan that would gain

him credibility with investors. It could include creating a central bank, converting the ruble, and getting Moscow's ballooning budget deficit under control.

In Moscow, Bush will throw in some sweeteners of his own. He's ready to say he'll offer the long-deferred U.S.-Soviet trade agreement to Congress for ratification, setting the stage for most-favored-nation tariff status for the Sovi-



ets. Bush also is likely to call for raising the current \$300 million ceiling on Export-Import Bank loan guarantees to U.S. businesses selling to Moscow. And Bush will bring a proposal for expanded technical assistance—worth as much as \$15 million next year—to help the Soviets develop their energy sector, convert defense factories to civilian production, and boost agricultural output.

Gorbachev is likely to welcome the

help—and use it against hard-liner critics. They recently blasted him for abandoning sacred communist principles and threatened to force a vote on his performance as party chief at a plenum on July 25. Support from the U.S. and other countries, says Ernest Obminsky, deputy Soviet foreign minister, "is now of the utmost importance to the internal situation in the Soviet Union."

While the Kremlin is preparing to take such steps as privatizing the huge, state-owned maker of Lada passenger cars, it's far from clear that Gorbachev understands the potential of his new links to the West. Any doubts were heightened on July 23, when Gorbachev announced his intention to seek full membership in the IMF and World Bank. The West believes that Moscow must make far more progress on reform first, but the Soviets are impatient. Says one State Dept. official: "An IMF [reform] program without any real cash behind it is not going to be very enticing to Gorbachev."

POTSHOTS. Bush, who is well aware of just how far down the reform road Gorbachev must go, is approaching U.S.-Soviet economic ties cautiously. But even his measured entente is drawing fire from the right, so he will likely try to deflect some of these potshots by trying to teach the Soviets Western values. He plans to deliver major speeches on democracy and free markets. He'll hobnob with Russian Republic President Boris N. Yeltsin and will reassert support for the Baltic states. And in Kiev, he'll demonstrate support for religious freedom at the site of a Nazi massacre of thousands of Jews.

If all this sounds a bit anticlimactic, it is. But that's only because the U.S.-Soviet relationship has matured to the point where jaunts from Washington to Moscow are no longer the stuff of high drama. Among the least intoxicated by the big show in Moscow will be U.S. executives. They'll be less interested in the summit communiqué than in the fine print of a slew of promised reforms that could finally clear what stands between them and big deals in the Soviet Union.

By Bill Javetski in Washington, with Rose Brady in Moscow

MEETING IN MOSCOW: THE AGENDA

ARMS CONTROL

As the summit's centerpiece, Bush and Gorbachev will sign the Strategic Arms Reduction Treaty, cutting nuclear arsenals by 30%

TRADE

Bush plans to announce he will propose most-favored-nation trading status for the Soviet Union. He will also pledge improved trade with the Baltic republics

ECONOMIC LINKS

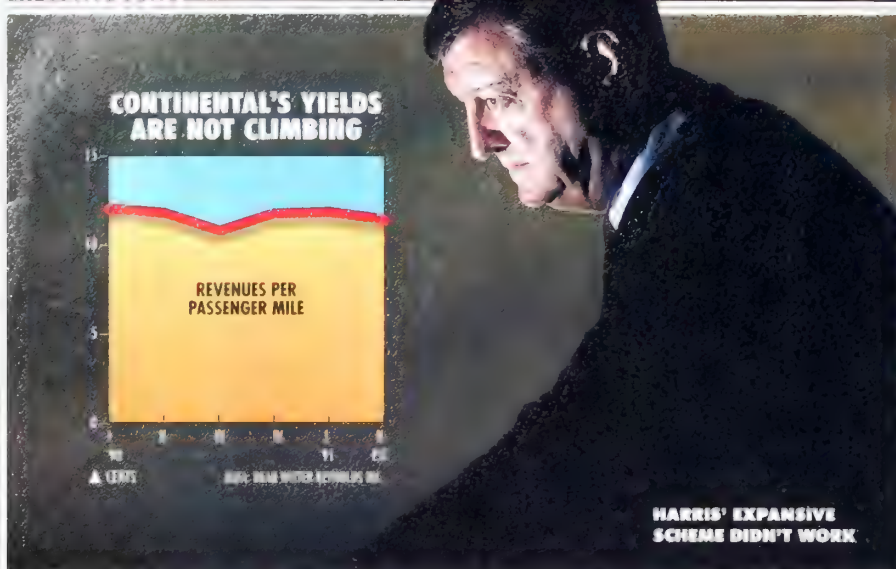
Bush will announce an expanded program of U.S. technical advice to Moscow on areas ranging from agriculture to energy development

BRANCHING OUT

To build ties beyond the Moscow central government, Bush will meet with leaders of the Soviet republics, most notably Russian President Boris Yeltsin

REGIONAL ISSUES

Bush and Gorbachev will discuss U.S.-Soviet cooperation in encouraging a Middle East peace conference and policing Iraq



THE MESS AT CONTINENTAL: 'WE HAD TO CHANGE COURSE'

A new Chapter 11 restructuring plan may mean layoffs and asset sales

Bankruptcy is never pleasant, but for Continental Airlines Chief Executive Hollis L. Harris, Chapter 11 is becoming more and more agonizing. Since putting the carrier into Chapter 11 bankruptcy reorganization in December, the former Delta Air Lines Inc. president has tried to fly Continental out of its mess—growing in some markets and vowing to avoid layoffs. But the effort hasn't worked. While all carriers have been hurt by a sluggish market, Continental Airlines Inc. has been clobbered. By early July, after months of red ink, "we saw it was worse than we thought," says a person involved in board deliberations. "We knew we had to change course."

That may be an understatement. As part of a shakeup, the board has abandoned Harris' plans. While Harris will still be CEO, new Executive Vice-President Robert R. Ferguson III, a veteran of the Braniff Inc. and Eastern Air Lines Inc. bankruptcies, will be calling many of the shots. He was brought in from Continental's holding company and will report to Harris. But Ferguson has a mandate from the board to make changes as he sees fit.

SWIFT SHIFTS. Continental executives and people outside the airline with knowledge of its operations say that Ferguson is preparing a restructuring program that could include layoffs, big asset sales, and even some departures from

certain markets. Says one lawyer who has dealt with both Ferguson and Continental: "Changes will be swift and far-reaching."

Harris, who declined repeated requests for comment, may not have steered Continental out of its mess, but he can't be blamed for landing it there. When Continental filed for Chapter 11, it was reeling from high fuel prices, heavy debt, and a legacy of poor management under Frank A. Lorenzo. Yet Harris did anything but retrench.

His rationale: Continental risked losing passengers unless it demonstrated it was more than just a liquidating entity, à la Eastern. Harris boldly expanded in some markets. In New York, he took over 11 planes and 64 landing slots from Eastern at LaGuardia Airport, making Continental the largest carrier in the area, with 344 flights a day. And while he matched rivals' fare cuts, he resisted big cost-cutting measures and refused to order layoffs. Why? "Everyone figured that after the [Persian Gulf] war, things

Ferguson will review everything—and may abandon unprofitable routes or even such hubs as Denver

would bounce back to normal," says Continental executive.

Harris may have hung on too long. Even as Continental was being hampered by sluggish traffic and fare wars, Harris "kept operating like he was Delta," says a former senior executive. "Costs got out of control."

FARE FIASCO. The costs wouldn't have been so onerous if Harris had attracted more full-fare business travelers. Instead, bargain hunters bought up seats on the cheap. As a result, while the average plane was 70% full in June, says Continental, yields—revenues per passenger—remained weak (chart). And valuations, such as Northwest Airlines Inc., continued to slash fares.

In early July, Continental tried a fare increase. But when no competitor followed suit, it was forced to rescind the hike. The reversal wasn't just embarrassing. It also suggested strongly that Continental would be hard put to turn a decent profit in the normally strong summer quarter.

The weak returns distressed Minneapolis investor Carl R. Pohlad and other board members, say two people privy to the board's deliberations. So directors turned to Ferguson, Lorenzo's former right-hand man, who had tried to steer Eastern through Chapter 11. Directors were aware that it might appear that Lorenzo was behind the decision to bring in Ferguson. But while Lorenzo is on the board, he doesn't sit on the executive committee calling the shots. And appearances aside, the board felt it had little choice: Harris had already gotten rid of most of the Lorenzo-era staffers who knew the bankruptcy courts.

Now, Ferguson, as vice-president of finance and marketing, will review nearly every major cost, including marketing, which had scant control under Harris. Creditors say Ferguson may abandon unprofitable markets or even such hubs as Denver, where Continental has struggled against United Airlines Inc. Neither Harris nor the company is giving specifics, but a spokesman says, "We'll be reviewing everything."

Continental isn't about to crash. The court recently approved a loan package that will give it nearly \$100 million in fresh cash, and it has begun cutting costs. And it has strong-armed its lenders into kicking in money for plane refurbishments and restructuring, deferring saving it about \$300 million. Still, it has to cut much deeper before it can hammer out a reorganization plan. If it does, it might emerge from bankruptcy sometime next year. But the latest moves are the top signal that Harris is likely to be a co-pilot, at best, when that day comes.

By Mark Ivey in Houston

ICAHN'S CRAZY-LIKE-A-FOX BET FOR PAN AM

gambling that a deal, backed by American, will help TWA survive

ot one to be rushed or bullied, Delta Air Lines Inc. held back earlier this year as rivals American and United scrambled to pick up routes to Europe from failing carriers. In mid-July, Delta Chair-Ronald W. Allen calmly suggested a \$450 million deal for bankrupt Pan Am's expansive European routes and its Coast shuttle. Gentlemanly indeed.

so fast. American Airlines Inc. and financier Carl C. Icahn, chairman of Trans World Airlines Inc., are going for a brawl. On July 22, Icahn announced a crafty \$450 million deal for nearly all of Pan American Airways Inc. (tapped). While Icahn's buyout—given TWA's red finances—is questionable, American muscle means Pan Am creditors can't dish him out of hand. American has agreed to \$250 million worth of Pan Am's assets to Icahn if he can off the deal.

en with American's wing, Icahn faces enormous hurdles. Delta and United Airlines are prepared to buy nearly all of Pan Am for a combined \$1 billion. Icahn may find that hard to beat as he struggles to restructure TWA's \$4 billion debt. Creditors often to repossess assets and engines. Icahn is clearly gambling on other people's

," says Steven Tanenbaum, a TWA advisor. Toughest of all: The TWA-American deal must win favor with the bankruptcy court and regulators, who see dangerous competition in the skies.

P CARD. Icahn is gambling that the American deal could help solve his problem at TWA. He figures that creditors have nothing to gain by forcing him into bankruptcy court. Instead, if the Pan Am deal succeeds, TWA bondholders gain

prized assets of a top rival. Even if the larger TWA isn't viable over the long haul, Icahn will have more time to liquidate. He vows to put together within a few months a prepackaged Chapter 11 filing that would force holdouts among TWA's bondholders to go along with his plans for slashing debt. Says Icahn: "This is the way to survive."

American, by contrast, has little at

At the least, American has temporarily thwarted its two major rivals and could make them pay more for key routes. American has already made Delta effectively raise its bid. Negotiators now say Delta would agree to take fewer routes and fewer of Pan Am's Airbus A310s in a deal, but pay the same price. United is making a separate bid for Pan Am's Latin American operations. American has a stronghold there, and to take up the challenge, United now has boosted its tentative offer by \$45 million, to \$235 million.

'IN THE BANK.' Robert L. Crandall, American's chief executive, fumed that, at \$290 million, Pan Am sold its London routes to United too cheaply. American recently paid \$445 million for three of TWA's routes to London. "They started off very stupidly," in the London route sale, Crandall says. "When you start stupidly, it's hard to finish smart."

While Pan Am creditors are wary of Icahn, they're cheered by the bidding. "If Delta wants to stay in the game, they need these routes," says Robert W. Kneisley, an aviation lawyer in Washington. Delta now isn't ready to budge much. "What you have is a very complex, highly conditional proposal from TWA vs. ours, which is backed up by money already in the bank," says Delta spokesman William Berry.

But even skeptics concede Icahn's deal promises something for everyone. Besides buying assets, Icahn would round up \$140 million from other investors for a reorganized Pan Am that would consist mostly of the Latin American operations. Creditors would get a stake in the new company. "Bondholders want to save face. They want

a piece of paper that says they have equity in a new entity that could make some money," says one creditor.

Still, Delta could easily top TWA with its deeper pockets and rock-solid credibility. The question now is whether gentlemanly Delta will have to get into a bare-knuckled fight.

By Wendy Zellner in Dallas and Todd Vogel in New Haven, with Chuck Hawkins in Atlanta and bureau reports



DELTA CEO ALLEN



AMERICAN CEO CRANDALL

RIVAL PLANS TO BREAK UP PAN AM

DELTA'S PROPOSAL

Delta would get:

- ▶ New York-to-Europe service
- ▶ Pan Am Shuttle
- ▶ Frankfurt hub
- ▶ Miami-London and Detroit-London routes

Pan Am would get:

- ▶ \$260 million
- ▶ Possible financing from Delta
- ▶ Obligation to honor tickets issued by Pan Am on routes it sells through Feb. 1, 1992

TWA/AMERICAN'S PROPOSAL

American would get:

- ▶ Pan Am's routes and facilities in Italy, Spain, and Portugal
- ▶ Pan Am Shuttle

TWA would get:

- ▶ Pan Am's routes to London from Miami and Detroit
- ▶ Frankfurt hub
- ▶ Eastern European routes
- ▶ Landing slots at New York's LaGuardia and JFK and Washington National

Pan Am would get:

- ▶ \$310 million for assorted assets
- ▶ \$140 million equity infusion to reorganize
- ▶ \$60 million in financing from TWA

DATA: BW

risk in this high-stakes game. At best, it could plug a hole in its growing European operations with Pan Am's routes to Italy, Spain, and Portugal. And the Pan Am Shuttle could feed traffic to American's international routes and open valuable space for American at crowded airports in New York, Washington, and Boston. Some analysts figure these assets may be worth at least \$25 million more than American is offering.

REVENGE OF THE NERDS IN BIOTECH LAND

Quiet little Chiron is set to bag Cetus—and the synergy could be great

They've been next-door neighbors for a decade in little Emeryville, Calif. But biotech outfits Chiron and Cetus are as different as tortoise and hare. Chiron Corp.'s nerdy scientists toiled quietly on modest projects. Cetus Corp.'s outspoken chief, Robert A. Fildes, wheeled and dealt in the lime-light. But on July 22, Chiron proved Aesop right again: Chiron agreed to buy Cetus for \$650 million in stock.

Investors begrudged the tortoise its victory lap. In part because the deal will help Chiron lose at least \$15 million next year, its shares sank 6 to 54%, while Cetus' tumbled 2% to 15%. Ominous signs, since shareholders must vote on

partners for royalties, even when that meant licensing potentially valuable technology. "We have not engaged in hype but in building value," says Chiron CEO Edward E. Penhoet.

That's not the kind of approach that puts companies on magazine covers. Indeed, the Street routinely criticized Chiron for a murky strategy and too many complex relationships. And products from Merck, Novo/Nordisk, and Johnson & Johnson's Ortho that use Chiron technology now reap more than \$600 million in sales. That makes the \$6.8 million Chiron earned last year on \$78.5 million in revenue seem paltry.

Yet ever so slowly, Chiron has been

watch from the sidelines for so long now may be able to buy assets cheap from players who weren't so patient such as Cetus. Since Fildes took helm in 1982, Cetus raised about \$8 million. Fildes spent most of it on top-grade facilities, a marketing organization, and research. But last summer, Cetus hit a wall: An advisory committee of the Food & Drug Administration sent Cetus back to collect more data on its flagship anticancer product, Interleukin-2. Fildes criticized the FDA, but within weeks, he had quit.

NEAT COMBO. Il-2 put such a cloud over Cetus that few wanted to rescue it. But Penhoet and Chiron Chairman William Rutter saw in it a startling array of assets useful to Chiron—most especially a brand-new, fully certified manufacturing plant just down the street. Chiron can quickly convert it to purify and package several products in its pipeline, including vaccines for AIDS and herpes. Moreover, Cetus' cancer business has several drugs in development besides Il-2. And since both companies work

with the immune system, Rutter believes Cetus' work will dovetail with Chiron's to make cancer treatments.

Ironically, one reason Chiron's stock has taken such a beating is that Cetus simultaneously is shedding a highly regarded technology called PCR for \$300 million to Hoffmann-La Roche Inc. Some investors are griping that it was Cetus' crown jewel, but that's far from certain. "PCR is a very promising research technology, but the commercial applications are still unclear," notes industry analyst Carol V. Hall of BioVenture Consultants. Adds Sutro & Co. analyst Margaret McGeown, "Chiron is probably better earning interest on that \$300 million."

If the deal gets done, Chiron will double its cash hoard to \$600 million and get a plant analysts say is worth \$75 million. That means roughly \$275 million—less, if Chiron's stock keeps dropping—buys everything else in a decade of research, a 50-person sales force in the U.S. and Europe, a \$30 million generic-drug business, and Il-2. In spite of its setback, the drug is expected to win approval next year and could generate at least \$30 million in annual revenues. One industry veteran is convinced the deal "is an absolute steal for Chiron." Tortoise, you've done it again.

By Joan O'C. Hamilton in Emeryville, Calif.



PENHOET AND RUTTER: TOP RESEARCH, PROMISING DRUGS

STEPS TOWARD CHIRON'S SUCCESS

- 1981** Chiron licenses hepatitis-B vaccine technology to Merck
- 1984** First to clone and describe genetic sequence of AIDS virus
- 1986** Hepatitis-B vaccine approved for marketing by Merck. Chiron forms joint venture in vaccines with Ciba-Geigy
- 1988** Discovery of hepatitis-C virus. Chiron and Ciba-Geigy begin testing AIDS vaccine
- 1990** Chiron expands ties to Johnson & Johnson unit to screen blood with its technology; turns first profit, \$6.8 million, on \$78.5 million in revenues

DATA: BW

the deal this fall. Yet if it gets the green light, investors could find Chiron to be superbly positioned.

Unlike many of its competitors, Chiron spurned the 1980s biotech wisdom of settling for nothing less than life as a fully integrated pharmaceutical company. While such talk helped Genentech, Amgen, and certainly Cetus raise hundreds of millions of dollars, Chiron had more modest goals. Its top brass, highly regarded scientists from the University of California, concentrated on what they did best: science, specifically cutting-edge work on infectious diseases and viruses. They were happy to work with

gaining ground and racking up a string of research achievements and business ties (table). Add a slew of promising new products and some of Cetus' hidden assets, and Chiron is ready for big things.

The company's way of getting along with partners may be one of its top strengths. It has a 50-50 joint venture with Ciba-Geigy to sell vaccines and a blood-screening business with Ortho. Also, it's working with a handful of other big drugmakers to develop new compounds based on so-called rational drug design technology. In these and other deals, Chiron has spread its risk.

And because Chiron was content to

YOU CAN'T BARGAIN WITH A STRIKER WHOSE JOB IS NO MORE

Many companies know exactly what they think about the bill to ban permanent replacement workers in strikes, which the House of Representatives passed in mid-July. They see it as labor's attempt to use its muscle to regain the muscle it has lost at the bargaining table. True enough, companies are desperate to reverse their slide. And the fear of losing their jobs has forced many union members to think hard about taking on management. But the issue can't be so easily dismissed. At stake is the central tenet of the U.S. enterprise system. In 1935, the Wagner Act laid out rules on collective bargaining in order to govern the relationship between labor and management. Key elements of the law are the rights of workers to form unions and to bargain collectively—rights that mark the fundamental distinction between U.S. unions and the labor laws found until lately in the East bloc.

The question labor raises is whether taking away strikers' jobs differs from firing them, which everyone agrees is illegal. And in the legal justification for permanent replacements, the Supreme Court has never directly addressed the question—much less answered it. The current law stems from a 1938 Supreme Court case called *National Labor Relations Board vs. Mackay Radio & Telegraph Co.* The dispute didn't involve permanent replacements. Instead, it was about Mackay's decision to move 11 nonstriking workers from its Los Angeles and Chicago plants to fill in for strikers in San Francisco. When 5 of the 11 wanted to return after the walkout ended, Mackay rehired five strikers.

ABLE-TALK? The union charged that management illegally discriminated against the strikers because of their strike activity. The court agreed, forcing Mackay to rehire the strikers. But the court added that in cases where management has committed no illegal acts, the company "is not bound to discharge those hired to fill the place of strikers, upon the election of the strikers to resume their employment,

in order to create places for them."

In short, you can't fire strikers, but you don't have to hire them back. That contradictory position, thrown out as an afterthought in a hypothetical statement, is the sole basis for the Supreme Court's stance on whether replacement workers conflict with the right to strike. The Court since has issued more than a dozen rulings on the subject,

the view that permanently replaced strikers haven't lost their rights completely. John S. Irving, a former general counsel of the NLRB who's now a management lawyer, points out that companies must give permanently replaced strikers first shot at new openings after the walkout ends. "And the vast majority of strikers are returned to their jobs by a preferential hiring list," he asserts.

Even if this were true, it doesn't explain why strikers should have to wait months or years to get their jobs back simply because they exercised a right. What's more, few strikers got their jobs back in the more prominent cases involving replacement workers (table).

Some managers argue that they're not penalizing employees for striking when they hire permanent fill-ins; they're just protecting the company's viability. But that boils down to an irrelevant question of intent. The striker has lost his or her job, no matter what reason managers give. "For most practical purposes, it's a distinction without a difference," says Paul C. Weiler, a professor at Harvard Uni-

versity Law School. "If a company discriminated against blacks or women and said: 'We didn't fire them, we just permanently replaced them,' it would get laughed out of court."

Opponents say that the proposed law would tilt the balance between labor and management toward the unions. But everyone agrees that management can hire replacements. The issue is whether it should offer them a permanent job. If you take away strikers' jobs for good, unions can't surrender. They can't simply give in, accept concessions, and go back to work. With no alternative, unions try to destroy the company, as they did at Eastern Air Lines Inc. Negotiation becomes an all-out, bet-the-farm war—precisely what the collective bargaining process is supposed to avoid.

Most executives are loath to give unions any ground. But an honest look at permanent replacements leads to one view: take away strikers' jobs, and you take away their right to strike.



each time citing Mackay. "The Supreme Court has never addressed this question," says Charles B. Craver, a professor at George Washington University's law school. "I don't think it has ever done an adequate job of balancing the interests of employees and employers on this subject."

Nor can legal experts explain the difference. The best attempt seems to be

WHERE STRIKERS LOST JOBS

Company	Year of walkout	Strikers*	Back at work*
PHELPS DODGE	1983	1,700	0
CHICAGO TRIBUNE	1985	825	90
HORMEL	1985	900	266
INTL. PAPER	1987	2,200	511
EASTERN*	1989	16,900	1,613
GREYHOUND	1989	5,600	0

*Excluding those who crossed picket lines

**Shut down 1/91

DATA: BW

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COMPUTERS

UNISYS IS BAILING FASTER

Job and product cuts will buy it time—but the debt is still 'killing'

James A. Unruh vowed to "transform" ailing Unisys Corp. when he took over as chief executive 15 months ago. He shook up top management, scrapped the expansionist visions of predecessor W. Michael Blumenthal, and began cutting jobs and selling assets. But with sales diving all across the computer industry, drastic steps haven't been enough.

In fact, transfusion, not transformation, may soon be the order of the day at Unisys. On July 23, Unruh unveiled plans to cut 10,000 jobs by mid-1992, shrinking the Blue Bell (Pa.) computer maker to 60,000 staffers, fewer than half the head count when Sperry Corp. and Burroughs Corp. merged to form Unisys in 1986. He'll also trim the number of products Unisys sells, and he'll market them to fewer industries. The

cost of the changes: a dizzying \$1.2 billion write-off, resulting in a \$1.3 billion loss for the second quarter. Says the genial North Dakotan: "This is not a fun time, certainly."

For all their impact, the cuts don't represent a strategic shift so much as a play for time. They will help Unruh keep the bankers at bay while buyers—possibly including Japan's Toshiba Corp.—look over various divisions. Because of persistent losses, Unisys in June grew perilously close to violating the net-worth covenants attached to a vital \$1.25 billion credit line. The pruning has persuaded the company's bankers to cut their net-worth requirement from \$3.5 billion to \$2 billion through January, 1993. Staying ahead of the lower target will keep Unruh out of more renegotiations or bankruptcy court. Unruh says they should even be enough to produce a profit by yearend.

Now, Unruh can work harder on par-



UNRUH: POSTING A \$1.3 BILLION LOSS FOR THE SECOND QUARTER

ing \$3.8 billion in long-term merger debt. Unruh has been hard-pressed to sell enough business units and real estate to work the debt down. Buyers are bargaining hard for such assets as the Time Inc. computer-networking company, which a Swiss buyer picked up in June for \$207 million in cash, down from the \$250 million in stock that Unisys paid in 1989. Unruh shaved about

\$300 million in debt in the second quarter, half the amount slated for the first year. Unruh says there's plenty more real estate that Unisys can sell.

OFF LIMITS. If the moves do deliver profitability, they could also make Unisys more attractive to a foreign investor or buyer. A deep-pocketed partner, such as Toshiba, is what Unisys needs to take care of its "killing" debt, says George Lindamood, an analyst with Gartner Group Inc. in Stamford, Conn. Such a buyer, he says, would get a big Unisys base of computer users and a foothold

DEALS

THE TROUBLE WITH BILL FARLEY: CHAPTER 7

Now, a bondholders' bankruptcy suit may unravel the financier's empire

In the end, it's the little things that count. With a wad of cash that Drexel Burnham Lambert Inc. drummed up for him with junk bonds in the deal-mad 1980s, conglomerateur William F. Farley racked up some big buys. He laid out \$2 billion for Northwest Industries in 1985 and \$3 billion for West Point-Pepperell Inc. in 1989. But one of his smallest deals, the \$135.5 million sale in 1990 of metal former Doehler-Jarvis, is the one that now may lead to the dissolution of Farley's \$3.5 billion industrial empire.

Claiming that Farley's sale of Doehler-Jarvis to ICM Industries Inc. last July amounted to a "fraudulent conveyance," holders of \$172 million of Farley Inc. bonds on July 24 marched into federal court in Chicago and sued to force Farley Inc. into bankruptcy. Fraudulent conveyance is a mouthful (page 74), but the creditors' complaints boil down to this: Doehler was the last Farley Inc.

operation capable of generating the cash to meet bond interest payments of \$29.4 million a year, and its sale left Farley with \$100 million of Doehler's pension and other liabilities. Moreover, the bondholders complain, Farley unfairly favored another creditor, Bank of New York, by paying it some \$90 million of proceeds from an Apr. 16 sale of Fruit of the Loom Inc. stock held by Farley Inc. "We tried very hard to do this without bankruptcy," says Wilbur L. Ross Jr. of Rothschild Inc., an adviser to the Farley bondholders' committee. "If diplomacy always worked, then there wouldn't be wars, either."

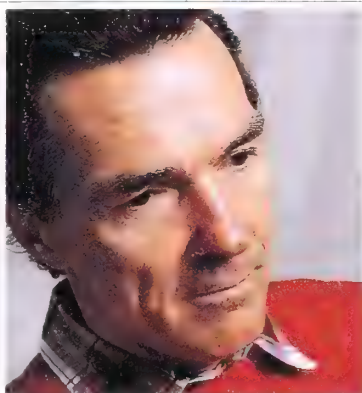
Farley declined to be interviewed. But in

a statement, he said that he had "preferred more in liquid value than the subordinated noteholders are likely to receive in a bankruptcy." The company, he added, will seek Chapter 11 protection.

FRUIT SALE. The bankruptcy petition doesn't directly implicate Farley Inc. operating units. But if the involuntary filing goes through and the typical Chapter 7 timetable holds up, some 18 months from now Farley Inc. may have to sell its crown jewel, 7.2 million shares in Fruit, to satisfy bondholders' demands. And despite Farley's painstaking efforts to insulate his various holdings, his hold on textile company West Point-Pepperell also is in jeopardy. The reason: Farley Inc. indirectly controls West Point. "This puts the whole ownership

situation in a very unstable position," says George Vanderheid, manager of two Fidelity Investments mutual funds that own large stakes in Fruit.

The Chapter 7 bankruptcy filing comes after weeks of talks between the bondholders and Farley over a \$100 million interest payment that he missed on Feb. 15. But the negotiations, which were



FARLEY MAY BE LOSING CONTROL OF HIS PRIZE FRUIT OF THE LOOM

...e, along with Unisys' highly re-
d mainframe technology.

...sys has close ties to Japan already.
... & Co. in June, 1990, invested \$150
... to acquire a special issue of Un-
referred stock, effectively giving it
... of the company's equity. And Mit-
...d Unisys each hold one-third own-
... in Nihon Unisys Ltd., a \$2 billion-
... Japanese computer marketer.
... would gain from a Unisys tie-up
... Toshiba, Lindamood argues, since
... Japanese companies are often busi-
... partners. What's more, recently ele-
... Unisys President Reto Braun, for-
... head of the company's Pacific-Asia
... n, has a Rolodex full of Japanese
... ts.

...re's one big roadblock to foreign
... l: Unisys' \$2 billion defense unit,
... is legally off limits to non-U.S.
... nies. But the defense business re-
... became profitable, making it
... salable to a U.S. buyer. One candi-
... Martin Marietta Corp. Unruh de-
... comment on any potential sales.
... ruh insists Unisys is not simply
... away. "We think we are a long
... from any such thing," he says. But
... ntinuing computer slump and stag-
... in defense spending increase the
... of Unruh getting more transforma-
... than he bargained for.

By Joseph Weber in Philadelphia

...mostly in New York, gradually
... d to a halt by mid-July. The two
... remained "tens of millions of dol-
... part," Ross says, on their valua-
... of a proposed bond buyback by
... r. Finally, on July 22, Ross phoned
... in Chicago and advised him that
... creditors' committee was about to
... mend the bankruptcy filing. "We
... eading into a litigation mode," Ross
... e told Farley.

...ically, Farley bondholders don't
... to be the big winners, even if
... prevail in court. Sure, they may
... re some value from their bonds.
... e big payoff is more likely to go
... e owners of Fruit of the Loom
... While Farley may retain his per-
... holdings of nearly 3 million shares
... uit, he'll lose most of his 43% inter-
... the company if he's forced to un-
... he 7.2 million shares owned by Far-
... e.

...upshot: Fruit shares, now trading
... d \$16, could surge once investors
... worrying whether Farley's parlous
... cial situation will hurt Fruit.
... s more, the underwear company,
... of a controlling shareholder, then
... become a takeover target. "I'm
... to win in this situation no matter
..." says Fidelity's Vanderheiden. No
... Bill Farley wishes he could say
... ame.

By David Greising in Chicago

THE LAW

LET IT BE? NOT ON YOUR LIFE

Remember Apple Records? Apple Computer can't forget

You say you want a revolution? Well, Apple Computer Inc. has certainly changed the world, not only for business professionals, but for such electronic experimenters as songwriters and musicians. Ironically, that has compounded Apple Computer's current times of trouble—to the tune of some \$38 million. That's the amount that the Cupertino (Calif.) company wrote off in the quarter ended June 28 as a reserve for a lawsuit against it by Apple Corps Ltd. In case you haven't dusted off your Beatles records lately, that's the holding company for the rock group's surviving properties. The reserve for the suit, once dismissed by Apple Computer as a nuisance, added to a charge of \$186 million for layoffs and relocations. That made Apple Computer lose \$53.1 million in the last quarter.

Here's the background: Apple Corps wants to maintain its trademark on the Apple name and logo in the music business. So two years ago, the British company, owned by the surviving Beatles and John Lennon's estate, filed suit in British High Court against its U.S. namesake. Apple Corps claims that Apple Computer is violating a 1981 agreement that bars it from the music business in exchange for permission to use the Apple name.

'THE GREEDLES.' That's no longer possible. Apple Computer's Macintosh is now used by electronic virtuosos from local garage bands to Bon Jovi to help compose, mix, and print musical scores—or even to play their synthesized sounds. David M. Kusek, president of music software company Passport Designs Inc., estimates that market to be at least \$100 million annually. Already, companies making musical software and hardware enhancements for the Macintosh say that the suit has caused Apple Computer to slow its own technical advances in this area and to back off on its marketing and advertising support for such products. That has raised the ire of musical technologists against the former rock sensations. "We call them the Greedles," grouses Christian Halaby, president of Opcode Systems Inc., a maker of computer software and hardware for musicians who use the Mac.

But musical computers are important for more than their ability to make composers and musicians happy. All computer companies are spicing up their systems by adding so-called "multimedia" technology, such as animation, video, and, yes, music. If Apple Computer has to avoid making similar moves, it could prove to be technologically crippling. "It just defies comprehension that Apple could allow itself to be repositioned as a unimedia computer," says W. Bingham Gordon, senior vice-president at



software maker Electronic Arts Inc.

Lawyers say that at first, Apple Computer simply tried to strong-arm the British company into dropping its trademark, simultaneously challenging its validity and offering the company a settlement on the order of \$10 million. "Apple Computer misjudged how serious Apple Corps was about its trademark," says Katherine C. Spelman, a partner in the San Francisco law firm of Townsend & Townsend.

Is a settlement imminent? Executives at both Apples decline to comment, but Apple Computer's reserve makes it seem so. Moreover, it's looking more and more as if \$38 million will be the price of what seemed like a shrewd business decision. Co-founders Steven P. Jobs and Stephen Wozniak have said they chose the name Apple to get the name in the phone book ahead of rival Atari Corp.

*By Richard Brandt in San Francisco,
with Mark Maremont in London*

EDITED BY HARRIS COLLINGWOOD

NCNB AND C&S TAKE THEIR MEDICINE

► How about a \$1 billion big bath before the big linkup? That's what NCNB and C&S/Sovran intend to do before joining forces as NationsBank by early 1992. The two Southern superregionals agreed on July 22 to a \$4.3 billion stock swap, creating a bank with \$118 billion in assets.

C&S/Sovran directors agreed to the merger after the magnitude of the bank's real estate lending debacle in Washington became clear. Nonperforming loans at C&S/Sovran already total \$1.3 billion, and \$600 million more in loan-loss provisions are likely to be tacked on before yearend. For its part, NCNB is expected to take a big write-down on its takeover loans. But by getting the bad news out of the way now, NationsBank's 1992 earnings should surge if the merger process is handled deftly.

TENNECO FILLS THE TOP JOB AT J.I. CASE

► Ending months of speculation, Tenneco named a former Deere & Co. executive to head J.I. Case, its troubled farm-and construction-equipment unit. Robert Carlson will replace James Ashford, who stepped down in March, just before Case reported a \$147 million quarterly loss. Carlson, 61, who spent 29 years at Deere, plans to whittle down Case's fat inventories. He'll also have to contend with a shareholder suit that charges that Case inflated sales figures last year. Tenneco had no comment on the suit.

CONCESSION TIME FOR THE STEELWORKERS?

► As the woes of the steel industry continue (page 20), the United Steelworkers (USW) is talking to Bethlehem Steel and USX (page 59) about possi-

ble concessions at several plants. Bethlehem wants cuts of up to 2,000 jobs, plus some wage reductions and work-rule changes, as part of its effort to modernize two structural steel plants. The union would get stock in a new joint venture the company plans to set up with British Steel.

At USX, a management-union task force is looking into the possibility of a union buyout of the company's 700-worker Chicago South Works. The plant, which also makes structural steel, probably will close if it isn't modernized. To make the deal work, the USW would need to make concessions, including job cuts.

CHARLES KEATING KEEPS LOSING FRIENDS

► When Charles Keating enters a Los Angeles state courtroom on Aug. 2 for his trial for securities fraud, he'll recognize many of his accusers. On July 22, former Lincoln Savings President Robin Symes pleaded guilty to state and federal securities-fraud charges, becoming the fourth former Keating aide to do so.

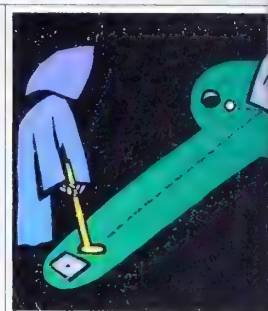
Symes is expected to cooperate with federal prosecutors, who are gathering evidence that could soon lead to an indictment of Keating. Symes also is expected to testify in the state criminal trial against Keating and co-defen-

MAY YOU PUTT IN PEACE

Back in the heyday of conglomerate, it wasn't unusual to find companies with a hand in everything from parking lots to space-age electronics. Such diversification is out of fashion, but that hasn't stopped Ahlgrim & Sons Funeral Home in Palatine, Ill., from running a miniature golf course in its basement.

Owner Roger Ahlgrim justifies the arrangement by noting that the 9-hole, par-23 course is booked months ahead. Funeral homes don't usually get so much advance notice. And Ahlgrim has a reason for not charging for use of the course. "It gets people comfortable with coming here," he says.

The course itself is a killer. On the first hole, golfers must putt around a skull. Elsewhere, a guillotine, spider webs, and tombstones remind golfers of their mortality. There's only one catch: No golf during services. Admits Ahlgrim: "I have to cancel lots of reservations."



dant Judy Wischer, a former president of American Continental, Lincoln's owner.

CIBA-GEIGY HOLDS THE LINE ON PRICES

► Victims of high blood pressure can already choose from six ACE-inhibitors—the newest treatment for their ailment. That's why the market's newest entrant, Ciba-Geigy, is offering price protection for buyers of Lotensin, its ACE-inhibitor that went on the market in mid-July.

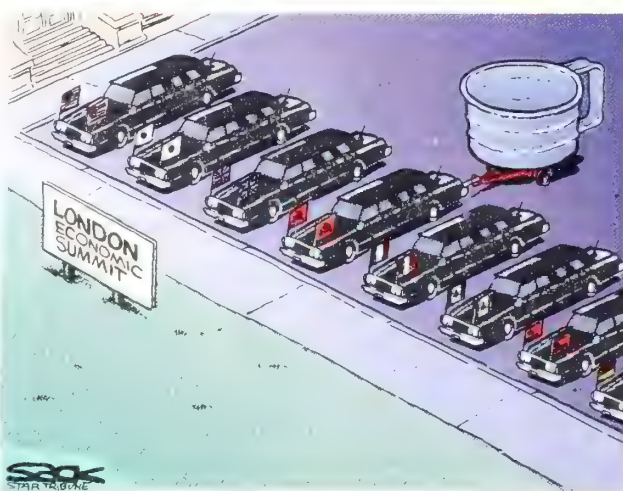
The plan works like this: A patient pays the wholesale

price of the drug plus a standard pharmacy markup, ranging from 22% for a bottle of 30 pills to 5% for a 100-pill supply. In future years, Ciba-Geigy will reimburse patients for any price increase of 10% and above that initial charge. The offer is a gamble, since the drug will have to meet or beat the annual sales projection of \$100 million if Ciba-Geigy is to make a profit on the scheme.

BUSINESSLAND: HOLD EVERYTHING

► JWP's proposed acquisition of computer retailer Businessland is hitting last-minute snags. First, Businessland bondholders forced JWP to restructure its bid. Then, on July 24, retailer ComputerLand made a competing offer for Businessland.

JWP is offering \$1 per share in cash for up to 53% of Businessland's stock, while privately held ComputerLand is offering to swap \$1 worth of newly issued stock for each share of Businessland. And ComputerLand is offering bondholders 45¢ on the dollar, 10¢ more than JWP. Although initially rejected by Businessland, ComputerLand says it will keep its offer open on a friendly basis.



SAM NUNN IS FLAPPING HIS HAWK WINGS AGAIN

By leading Democratic opposition to the Persian Gulf War, Senate Armed Services Committee Chairman Sam Nunn had his hawk's feathers singed. Now, the Georgia Democrat may have found a strategy to regain his stature as party's preeminent voice on defense policy.

Nunn is leading the charge for a new antimissile defense system for the U.S.—even if it requires renegotiating the 1972 Ballistic Missile Treaty with the Soviet Union. With U.S.-Soviet tensions ebbing, many fellow Democrats think this is the wrong time to inflame Moscow over ABMs. Expanding missile defenses, says committee member Carl M. Levin (D-Mich.), “would leave us mired in the quagmire of the cold war.”

On July 17, the committee voted to back Nunn's plan to deploy an antimissile system at Grand Forks, N.D.—the only U.S. site allowed by the ABM treaty. The measure also directs the President to open talks with the Soviets to amend the ABM pact, a move that could permit additional antimissile sites and orbiting missile defense sensors.

Many liberals find the whole idea scary, says Nunn and the committee's rank-and-file Democrat, John Warner of Virginia, beg to differ. They contend that a new ground-based antimissile system is needed to shield the U.S. against accidental or unauthorized launches by the Soviets, or nuclear strikes by a future Saddam Hussein. The public fascination with Patriot missiles blasting Iraqi Scuds out of the sky makes the idea politically appealing. “People want to go into the election next year showing they're in favor of some kind of missile defense system,” says one Democratic Senate staffer. Nunn's idea is likely to pass the full Senate—perhaps in pared-down form—because it offers something for almost everyone. For Democrats opposed to tinkering with the ABM treaty, it seeks to assure compliance with the pact through

1996. To woo pro-Star Wars Republicans such as Warner, there's a promise to renegotiate the accord, deploy ABMs at several more sites, and fund research for the space-based interceptors called “Brilliant Pebbles.”

The House is another story. House Armed Services Chairman Les Aspin (D-Wis.) says it's premature to rewrite the ABM treaty. And the more liberal members of his committee will want their chairman to take a tough line against the Nunn measure in a House-Senate conference this fall. The House has already voted to slash Strategic Defense Initiative spending and kill Brilliant Pebbles. “This will kick up a big fuss,”

predicts a House Democratic staffer.

HANDY MAN. Arms-control advocates also are distressed by Nunn's move. “Why would a country fire ballistic missiles at the U.S., which would certainly provoke a devastating counter-attack?” says Spurgeon M. Keeny Jr., president of the Arms Control Assn. Adds John Pike of the Federation of American Scientists: “The threat is totally hypothetical.”

Even the White House is a bit queasy at the thought of the Senate fiddling with the ABM pact just as President Bush heads for Moscow to sign



NUNN WANTS A NEW ANTIMISSILE SYSTEM

the Strategic Arms Reduction Treaty (page 23). The Soviets have warned that they would walk away from START if the U.S. breaks the ABM agreement.

But this discomfort is likely to be temporary. The Administration remains committed to deployment of space-based missile defenses. Ultimately, that will require rewriting the ABM treaty. When the time comes, Bush will find Sam Nunn a handy man to have on his side. Meantime, Nunn's proposal for a new antimissile system serves to remind conservative Democrats that notwithstanding his Persian Gulf lapse, he's still his party's leading pro-defense voice.

By Amy Borrus

TAL WRAPUP

MINNEES

Supreme Court nominee Clarence Thomas has taken a lot of flak from congressional Democrats for his record of affirmative-action hiring. But Thomas' views on Congress' record as an employer could make critics squirm. As chairman of the Equal Employment Opportunity Commission, Thomas had harsh words for employers' refusal to apply federal anti-bias rules to themselves. And he championed the struggle of mainly black cafeteria workers on the Hill to unionize against congressional opposition. In a 1989 interview with BUSINESS WEEK, Thomas said: “I take to heart

James Madison's warning that the only way the legislature will prevent itself from tyrannizing the populace is to make sure that the laws it passes apply to the legislators themselves.”

CAMPAIGNS

Republicans, whose hopes for more seats in the Senate next year have been dimming, have a new and unexpected cause for worry. Internal GOP polls show that 20-year veteran Bob Packwood is in trouble in Oregon. The moderate Packwood faces a primary challenge from the right. Then he must take on Representative Les AuCoin, who has the solid support of Oregon Democrats.

BANKING

A match between John D. Dingell (D-Mich.), the overbearing chairman of the House Energy & Commerce Committee, and the erratic Henry B. Gonzalez (D-Tex.), chairman of the Banking Committee, would usually be no contest. But Gonzalez seems to be winning a spat over the banking panel's draft financial reform legislation. He appears to be forcing Dingell to retreat on a request for a General Accounting Office review of the bill's special-interest provisions. And Speaker Thomas S. Foley (D-Wash.) has put a September deadline on the Commerce Committee's review of the legislation.

PHILIPS' BIG GAMBLE

CEO Jan Timmer sets his sights on dominance in consumer electronics

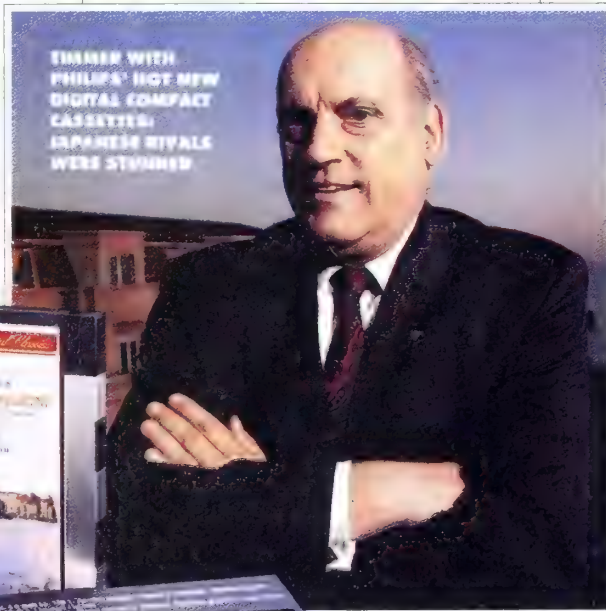
When Jan D. Timmer took over as chief executive officer of century-old Philips Electronics last July and promised a revolution, many rivals doubted it would ever happen. But suddenly, the makeover of the troubled Dutch technology giant is in full swing. Once notorious for slow-footedness in pushing products out of its labs, Philips under Timmer's sharp prodding has stolen a march on its Japanese rivals with a splashy new recording medium: the digital compact cassette (DCC), an audiotape system with crystal-clear sound.

Then, on July 23, Timmer rattled more cages when he struck a deal to sell off Philips' money-losing minicomputer division and its \$1 billion in sales to Digital Equipment Corp. for \$300 million to \$350 million. The message? He's dead serious about unloading the laggards in Philips' motley portfolio of businesses (table). While DEC thinks it's getting a good deal, the sale will rid Timmer of a major headache (page 36). Too small to survive on its own, Philips' minicomputer unit had racked up about \$250 million in losses in recent years. "Philips will sleep a lot easier with this one behind them," says a source involved in the deal.

SHOCK THERAPY. Timmer, who has earned a reputation as a freewheeling turnaround specialist in his 38 years at Philips, is moving into high gear on the biggest, riskiest project of his career. To revive the faltering \$28 billion company, which suffered a \$2.2 billion loss last year, the burly 58-year-old is in the midst of cutting \$1.2 billion in costs by slashing 55,000 jobs—nearly 20% of the work force. As if the firings weren't enough, Timmer has also cooked up a sweeping reeducation program known as Operation Centurion. It's

shock therapy to focus managers' minds on something that has been neglected at Philips for years: profits.

To fire up those profits in the 1990s, Timmer is betting more than \$2.5 billion on the DCC and other cutting-edge technologies. He's leaning on Philips' vaunted labs to spring high-definition TV, multimedia personal computers, and an ambitious entertainment and education system known as CDI over the next couple of years. At the same time, he is retrenching in businesses that once were the company's big hopes,



such as computers, semiconductors, and appliances.

In a series of rapid-fire moves, Timmer is turning to Japanese, American, and European rivals to provide technology too expensive for Philips to develop by itself. All told, it shapes up as a radical restructuring that will either restore Philips to its role as a global powerhouse or relegate it to a has-been. "Timmer's our very own Schwarzkopf," says a senior staff manager, "and he's driving a tank through the place."

Hanging on Timmer's efforts is the fu-

ture of the West's biggest maker of consumer electronics. Philips is the only European company besides Siemens that's a leading player across a broad spectrum of electronic technologies. If Philips can stake out a place in the sun for itself in the competitive 1990s, then Europe's indulgent research subsidies and trade policies will have been for naught. And increasing Japanese and American giants will have Europe to themselves. "We have to prove that Europe is not a second-rate power in electronics," says Einar Kloster, a director on Philips' management board.

Timmer will be riding a tiger as he strives to score big hits with a hot new products. The financial weakened Philips no longer has the financial muscle to absorb the kind of big loss it took on its bungled entry into VCRs in the early 1970s. The cash-cow lighting division that once was milked to fund research has had its margins trimmed in a price war with Siemens and General Electric. Already, interest charges on debt of \$7.5 billion sucked up 88% of last year's operating profits.

'ANOTHER CLIFF?' The savings from layoffs and asset-shedding alone almost guarantee improved earnings through 1992. First-quarter profits of \$68 million show signs of life surprisingly early. And although the net margin will still languish below 2%, analysts

expect profits to hit \$500 million for 1992. That includes the roughly \$175 million net gain from the July sale of its 47%-owned joint venture in household appliances with Whirlpool Corp. The rebound in Philips stock, by 60% to \$16 in the past 15 months, makes it one of Europe's hottest performers, though it still is at about half its 1986 peak. But unless Operation Centurion boosts productivity, "Philips could walk off another cliff by 1993," warns James Callaghan & Co. analyst William T. Coleman.

The management shake-up hits just as Timmer is readying a stream of risky new consumer-electronics technologies for the 1990s. Among his bevy of new products,



**PHILIPS HAS ALREADY
PLOWED \$250 MILLION
INTO HDTV
TECHNOLOGIES**

from Cannes to London flogging Philips products. He speaks Dutch, English, German, and French, but he speaks more English than his native language because he spends so much time traveling and trying to reshape Philips' global operations.

During the last year, a Timmer-directed series of Operation Centurion weekend seminars has gathered groups of top brass from around the world to brainstorm on mining more profits from their operations. "They come back as if they'd had a religious experience," says one lighting manager. "They hang up mottoes in their offices

has more immediate potential than digital compact cassette. Due out next in home, portable, and car models, DCC packs 90 minutes of sterling sound by using a revolutionary recording technique. The DCC's great selling point is buyers will be able to play their old, analog-tape cassettes on the new ones. The chief rival, a portable compact disc system called Mini Disc from Sony Corp., cannot play either existing CDs or cassettes.

According to industry observers say this war may lead to the kind of showdown

which Matsushita Electric Industrial Co.'s VCRs vanquished Sony's Betamax in the early 1980s.

If the history of the compact disc, introduced by co-developers Philips and Sony in 1982, is any guide, whoever wins this battle will also reap the benefits of speakers, receivers, and other audio components.

Philips is counting on the DCC to make up the flagging cassette market, where sales dipped last year for the first time. Cassette sales account for 46% of the recording industry's \$7.5 billion in sales, so soft sales worry Philips. Only Philips audio division is so its PolyGram recording division.

STRAITS. In short, Philips cannot afford to botch this one. It went over backward to line up the world leader Matsushita to develop and manufacture the products as well as music-industry giants EMI, Warner, Bertels-

mann, and its own PolyGram to provide the cassettes. It also signed the rock band Dire Straits to promote the technology on their world tour this year. In a sign that Philips may win out, even Sony recently said that it, too, might license the DCC in addition to pushing the Mini Disc. "So far," adds Paul Gluckman, managing editor of *Audio Week*, "Philips has made all the right moves."

If anyone can shake up stuffy, hide-bound Philips, it is Timmer. Unlike some other Philips managers, Timmer is constantly on the move, crisscrossing Europe

like 'Your client is your boss.'"

A new flow of profits will be essential if Philips is to pay for the products of the future. It has already plowed \$250 million into HDTV technologies and will probably spend another \$1.5 billion or more by the mid-1990s. The payback is far from certain.

BIRD'S SONGS. Another big absorber of funds is Compact Disc-Interactive, or CDI, which former executives estimate has sucked up \$500 million. This seductive new medium flashes text, graphics, sound, and video stored on an optical disc onto a TV screen. Using their CDI sets, which are expected to sell for \$1,000, toddlers will be able to tour the

Sesame Street neighborhood and play tunes on Big Bird's jukebox. Their parents will be able to play the St. Andrews golf course while getting tips from their favorite pro. Philips and Nintendo Co. have also teamed up to develop special CDI machines for video games.

Philips will launch CDI in the U.S. in October. But Philips will have to count on sales of the programming software more than on the players themselves—just as it makes more from PolyGram's CDs than from CD machines. Unfortunately, delays have turned off potential suppliers. There is also no assurance that couch potatoes want to interact with their TVs, as CDI requires.

Philips' CDI also runs the risk of competition from similar new features now emerging on mul-

HOW PHILIPS IS SLASHING ITS PORTFOLIO

Division	Share of total 1990 revenues	Share of total 1990 operating profit
 CONSUMER PRODUCTS TVs, audio, CDs, VCRs; PolyGram; personal and home appliances	45%	75.0%
 PROFESSIONAL PRODUCTS & SYSTEMS FOR SALE: Telecoms, defense, medical electronics, automation, PCs SOLD: Data processing to DEC for \$350 million	23	0.8
 LIGHTING Industrial, consumer, auto	15	18.5
 COMPONENTS Picture tubes, materials FOR SALE: Semiconductors	13	-0.5
 MISCELLANEOUS Matsushita components, Grundig electronics SOLD: Appliances to Whirlpool for \$610 million CLOSED: DuPont optical disks	4	6.4
OTHER INCOME	0	-0.2

DATA: COMPANY REPORTS, BW

timedia personal computers. To hedge its bets, Philips early next year will bring out its own new line of MPCs, used for everything from job training to splashy business presentations. Its success, however, hinges on executing ambitious plans to turn around its bleeding PC business first.

The high risks put all the more pressure on Timmer to make sure the newly set profit goals and work habits of Operation Centurion turn out to be more than just rhetoric. Philips' Japanese rivals say privately that the financially weakened Dutch

have been backed into a corner where they desperately need to score a big hit but have only a handful of new products. In their view, the odds are against Philips. "Philips' choices are limited," says an official of one big Japanese rival. "They have little freedom to experiment."

As a cagey insider, Timmer knows the Philips way well enough not to leave anything to chance. From the consultants he hired to lead Operation Centurion training seminars, say company union officials, he gets regular reports on his own managers

to make sure that staff cuts are made on the basis of performance rather than cronyism. "Timmer says it's now or never. If he fails, Philips dies," says Jost, a company researcher, who is chairman of the Philips workers' council in Germany. "And then we're all out on the street." As the old saying goes, there's nothing like the sight of a noose to focus the mind.

By Jonathan B. Levine, with Patricia Oster in Eindhoven, Neil Gross in Tokyo and Gail Schares in Bonn

DEC EXPECTS BIG THINGS FROM PHILIPS' MINIS

For a year now, slumping European operations have given U.S. computer makers nightmares. And none more so than minicomputer maker Digital Equipment Corp., which gets 40% of its \$13 billion in revenues and the bulk of its profits there. So, to make sure its profit engine doesn't sputter out, DEC is on a European spending spree that is on a par with that of the acquisitive Japanese.

The U.S. minicomputer company made its biggest play on July 23 with an agreement in principle to acquire Philips Electronics' \$1 billion minicomputer business. The purchase, at a bargain-basement \$300 million to \$350 million price, signals that DEC is no longer counting on growth from within to pull it out of its profit slump. Now, its brightest hope is to rekindle Europe, where revenue growth, although still robust, has slipped to 14% from the 25% rate of just two years ago. DEC's strategy, says Sanford C. Bernstein & Co. analyst Barry F. Willman, is simply to "buy business."

SWEET DEAL. The price was right for Philips' money-losing minicomputer unit. At just 30¢ to 35¢ for every dollar of sales, the deal costs half what DEC paid in December to acquire its 65% stake in its German joint venture, Digital-Kienzle Computer Systems. Philips' customers are largely small to midsize companies whose computer purchases are projected to grow at a rate of 12% to 14%, vs. 4% to 6% among large corporations. With Digital-Kienzle, and

now with the Philips bid, "we're looking for growth opportunities," says Wolfgang Jaeger, DEC Europe vice-president for strategic alliances.

DEC's plan is to turn Philips' minicomputer business into a reinvigorated distribution network. It would inherit Philips' customers, many in small retail banks and in countries such as Austria and Spain where DEC's current presence is minimal. Philips' customer base

way," says Paul Lethbridge, a vice president at market researcher INTEC Corp. European computer leaders IBM and Germany's Siemens could just as easily win over Philips' mini customers. DEC's latest restructuring charges all lend some urgency: With its U.S. operations hamstrung by recession and slower growth in Europe, DEC has laid off workers and closed plants to stanch the red ink.

The Maynard (Mass.) company's bid for Philips' unit comes amid a tough restructuring of struggling European computer makers. Last November, Fujitsu Ltd. acquired Britain's ICL and later added Nokia Data to its European

subsidiary. DEC has been among the most energetic of the Americans. In addition to the \$230 million spent for its stake in Digital-Kienzle, DEC recently bought up a small British financial-software house to aid its move into financial services. All told, DEC stands to add about \$1 billion in annual revenue from its European acquisitions. What's more, the company is now exploring joint research with Italy's Olivetti. And as a part of their talks, DEC and Philips are considering ties in PCs and semiconductors.

To make the transatlantic plan work, DEC will not only have to hold on to Philips customers, it will

also have to learn how to become a good European citizen. As part of the deal, DEC will pick up 7,000 Philips employees, all of whom want job guarantees. Before any deal can close, DEC must come to such an agreement with the employees' union—a foreign notion for nonunionized DEC. But DEC is betting that it will be able to restore some sparkle to one of the many Philips businesses that went flat.

By Gary McWilliams in Boston



A DEC DELIVERY IN FRANCE: EUROPE PROVIDES 40% OF ITS REVENUES

will also help DEC move away from slow-selling minis and instead peddle software and consulting as companies move off Philips' defunct mini line onto DEC machines.

But DEC will have to move fast. Philips has always sold at the periphery of its customers' business, selling computers that automate bank branch offices rather than headquarters, for example. "Philips is big in the financial and retail sectors but not in any controlling

INFLATION? DON'T EVEN SAY THAT WORD AROUND HELMUT SCHLESINGER

Bundesbank's incoming president is obsessed with rising prices

As he paces the beige carpet in his spacious office in the Bundesbank's concrete-and-glass headquarters two miles from downtown Frankfurt, Helmut Schlesinger looks remarkably relaxed—for a man who's about to take the hottest seat in global finance. But beneath the surface, he's anything but calm. Deeply disturbed by the prospect of reunification setting off a destructive "wage-price spiral" in Germany, the nation's incoming central bank president wastes no time stating his foremost concern. "Our task," he tells *BUSINESS WEEK*, "is to keep the value of the currency stable. That means avoiding inflation." That's a tough order. With reunification more than doubling the government's borrowing needs, to \$110 billion a year, Schlesinger's work seems to be cut out for him even before he takes over from Karl Otto Pöhl on Aug. 1. The money is continuing to expand, but inflation is heading toward its highest level in nine years (charts). Worse yet, Germany's current-account surplus is shrinking, and the proud German mark has lagged 17% against the dollar since 1989, raising the specter of more inflationary pressures.

HIKE? Amid such disheartening news, it's no wonder that many economists expect Schlesinger, the former Bundesbank chief economist and a dyed-in-the-wool monetarist hawk, to push Germany's high interest rates as much as a full point higher when the Central Council meets on Aug. 15. That move so might anger the U.S. and other European allies. But even though Schlesinger himself hints he might not be ready to move that soon, he is still likely to keep money tight well into 1992. "The 1970s showed there is no gain from inflation," he cautions. "There is a danger, however, that some people are forgetting this lesson." Here's one central banker who won't let them.

By Blanca Riemer and John Templeman in Frankfurt, with Igor Reichlin in Bonn



SCHLESINGER: "THE 1970s SHOWED THERE IS NO GAIN FROM INFLATION"

For months, Treasury Secretary Nicholas F. Brady has been complaining about the risks to the fragile global recovery posed by high German interest rates. Indeed, with those rates and the mark dominating the European Monetary System, ICI's Freeman believes Continental Europe may be doomed to "bloody weak" growth next year, perhaps only 2¼%.

With those concerns in mind, some observers think Schlesinger may become a little more flexible now that he is assum-

ing a global role. At the June 23 meeting of the Group of Seven industrialized countries in London, insiders say, Pöhl and Schlesinger reached a tacit understanding with U.S. and other allies to put a lid on German rates until fall if their counterparts would help brake the mark's rapid decline.

OPEN QUESTION. Not long after, the G-7 dumped dollars around the world, sending the greenback from a 19-month high of 1.84 marks to a level Schlesinger regards as "better for us," about 1.75. "A deal was made," says Michael R. Rosenberg, manager of fixed-income research at Merrill Lynch & Co.

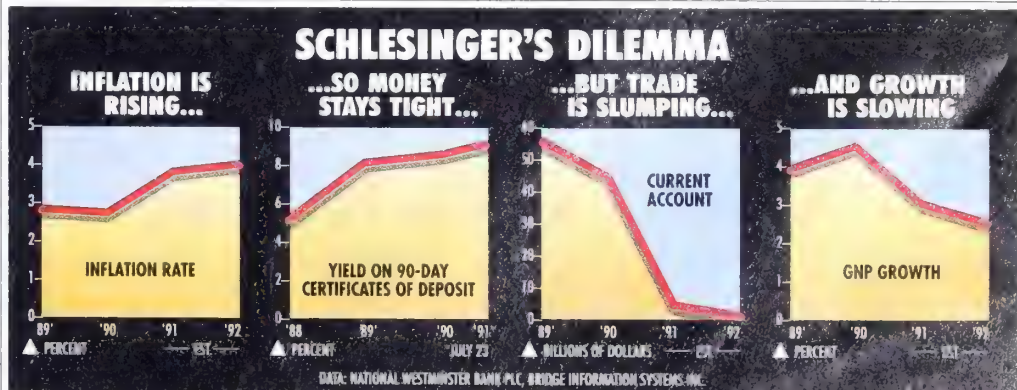
Whether Schlesinger can keep the lid on rates past September or October is an open question. July's \$10 billion tax hike to help pay for reunification probably will boost consumer prices by 4% for the month and will push the full year's inflation rate to 4.5%, estimates Commerzbank Chief Economist Jürgen Pfister. With big German unions already winning wage hikes of 6% to 7% lately, Schlesinger worries that workers will be asking for at least that much in 1992.

If these inflation jitters unnerve currency traders and send the mark reeling again, Schlesinger may have no choice but to boost the discount rate by a full point, to 7.5%, says Pfister. Others believe Schlesinger might instead revive a temporary surcharge on large secured loans to banks that was last used a decade ago. Such a plan would result in a "special Lombard" rate of 10.5%, 1.5 percentage points above its current level.

Still, some think Schlesinger would be wiser to leave rates alone. Every day, Schlesinger's office computer spews out statistics suggesting that Germany's nine-year upswing is finally faltering. And eastern Germany's economy is expected to shrink 20% this year.

Despite such indicators, Schlesinger is likely to stick to his hard line until he is convinced that price pressures are easing. "The 1970s showed there is no gain from inflation," he cautions. "There is a danger, however, that some people are forgetting this lesson." Here's one central banker who won't let them.

By Blanca Riemer and John Templeman in Frankfurt, with Igor Reichlin in Bonn



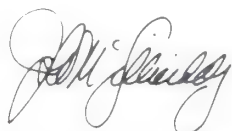
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WHY A PEACE DIVIDEND COULD LOOK PROMPTING TO TEL AVIV

The Israelis are casting it off as another propaganda ploy. But the surprise proposal of key Arab states to end their 43-year-old economic boycott in return for a freeze on settlements in the occupied West Bank and Gaza Strip trigger a badly needed influx of investment in Israel. If the Arab gesture is genuine, it couldn't have come at a better time for the Jewish state, which is barely coping with a massive influx of Soviet émigrés.

Already, the conciliatory murmurings from Israel's Prime Minister Yitzhak Shamir about sitting down with Arab leaders for a peace table are boosting the country's financial outlook: Jewish sent shares on the Tel Aviv Stock Exchange soaring from July 18 to July 23. "That's a sign of where things are going," says Sam M. Tocaty, chairman of Tel Aviv-based Aryeh Insurance Co.

URAGING. That may be just the beginning. If the boycott is removed, Israel suddenly becomes an attractive place for investment. Although the country is one of the world's most highly skilled—and inexpensive—work forces, large international corporations have hesitated there for fear of blacklisting in the Arab world. "The perception that Arabs might boycott is enough to discourage companies," says Bank of Israel Governor Michel Bruno. Net foreign direct investment last year amounted to barely \$200 million.

U.S. companies have stayed away in droves. A few exceptions: Intel, National Semiconductor, and Digital Equipment have important design facilities in Israel, where a potent tech, military-industrial complex has spawned thousands of engineers. "But where is GM?" asks Kenneth J. Bialkin, a lawyer who does Israeli-related work at New York law firm Skadden, Arps, Slate, Meagher & Flom. "Beyond a few tech companies, there's no one." And very few big European companies do business with Israel, even though France and Britain have antiboycott legislation, as does the U.S.

Now, says Bruno, "knowing that the Arabs themselves have lifted the boycott will be a green light for these firms." The results could be dramatic. Prior to this, the Japanese giants avoided Israel. But recently, teams from Japan's powerful Ministry of International Trade & Industry have been in Israel to look at investment opportunities, especially in high tech, while Japan Airlines Co. and El Al are negotiating a deal for direct flights between Japan and Israel.

A MAGNET? The European Community is offering Tel Aviv the potentially lucrative status of associate membership in the EC—if Israel shows political flexibility. That would guarantee tariff-free entry into the European market for Israeli products. With the Arab promise to remove the boycott, Israel could even become a regional magnet for investment.

Israel is going to need every investment dollar it can get. Even with a Middle East peace, Israeli government officials say there will be no reduction in multibillion-dollar defense outlays. Settling and providing jobs for the estimated 1 million Soviet émigrés expected to arrive by 1996 is likely to cost up to \$50 billion over the next five years, according to the Bank of Israel. With unemployment already close to 12% and inflation at 20%, fueling economic growth won't be easy.

But after four decades of hostile relations with the Arab nations, Israel is not quick to believe in Arab sincerity on this or any other issue. Even though it's under mounting pressure to sign off on the U.S. plan for an international peace conference, the Shamir government is still very uncomfortable with the idea of trading territory for political or economic gain.

The boycott offer, says Israeli Defense Minister Moshe Arens, "is more like a maneuver than a sincere offer." But as peace talks break out—if not peace itself—big companies are busy rethinking what Israel may have to offer.

By John Rossant in Rome



INTEL: A RARE U.S. COMPANY IN ISRAEL

AL WRAPUP

SOUTHEAST ASIA

Southeast Asia should be reveling in peace and prosperity. Yet, anxiety is rippling through the region. As Washington cuts back its military presence in the Pacific and forges a North American trade bloc, the leaders of Southeast Asia are hotly debating whether to form an economic bloc and security alliance of their own. America's clout already is slipping. It was the message coming from the July 19-22 meeting in Kuala Lumpur of foreign ministers from the Association of Southeast Asian Nations (ASEAN) and attended by Secretary of State James Baker. To demonstrate

their own economic might, the ministers endorsed a proposal to make ASEAN a "free-trade zone" within a decade. They also promised to study schemes for further economic integration, including a plan by Malaysian Premier Datu Seri Mahathir Mohammad, the firebrand of this new Asian self-assertiveness. He is calling for an East Asia Economic Group that excludes the U.S. It's not quite Fortress Asia, but the tone of the talks gave a U.S. observer reason to fear that this may lead to "a unified front against the U.S."

Talk of a new security alliance that may include the Soviet Union and China makes the U.S. even more jumpy.

Baker assured the group that the U.S. military commitment is firm and that the Pacific is safeguarded by bilateral treaties and regional alliances. But after announcements of U.S. troop withdrawals and the closing of volcano-stricken Clark Air Base in the Philippines, the Asians are moving to fill the vacuum, amassing their own high-tech arsenals. They are worried about potential flashpoints, such as the oil-rich and heavily fortified Spratly Islands contested by China, Vietnam, Malaysia, the Philippines, and Taiwan. As Southeast Asia flexes its new political muscle, Washington can no longer expect to call all the shots.

By Pete Engardio in Kuala Lumpur

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FINANCIAL BUSINESS

ARE YOU REALLY INSURED?

QUESTIONS YOU SHOULD ASK ABOUT
YOUR COVERAGE AND BENEFITS



Life insurance has long seemed a potent and benevolent force in society, faithfully dispensing retirement and death benefits down through the generations. Americans, who spend 5% of disposable income on life insurance, trusted that their policies were grounded in a bedrock of solid investments. And with \$1.4 trillion in assets, the U.S. insurance industry appeared well-equipped to keep on delivering.

Talk about nasty surprises. Along came the collapse of Executive Life, First Capital, and Monarch, whose foundations turned out to be crumbling junk bonds and real estate investments. And on July 16, Mutual Benefit Life Insurance Co. in Newark, N.J., with \$13.8 billion in assets, became the largest insurance failure in history. State regulators, charged with keeping the insurance industry solvent, have seized the errant foursome. That has left thousands of policyholders sitting in limbo, wondering what will become of their benefits. No one knows which insurers will be next. "Nothing of this magnitude has ever occurred before," says Daniel R. Gattis, senior vice-president at SEI Corp., a pen-

sion-fund consulting firm. "And it's happening so fast. Bing, bang, boom."

Over and beyond the 156 million Americans covered by life insurance policies, the crisis touches 15 million annuity holders who are counting on their insurance companies to furnish a secure retirement. Then there are the millions of people who invested in insurer-run products known as guaranteed investment contracts (GICs) through their company-sponsored 401(k) or other pension plans. Unlike banks and thrifts, government guarantees for insurance products are skimpy.

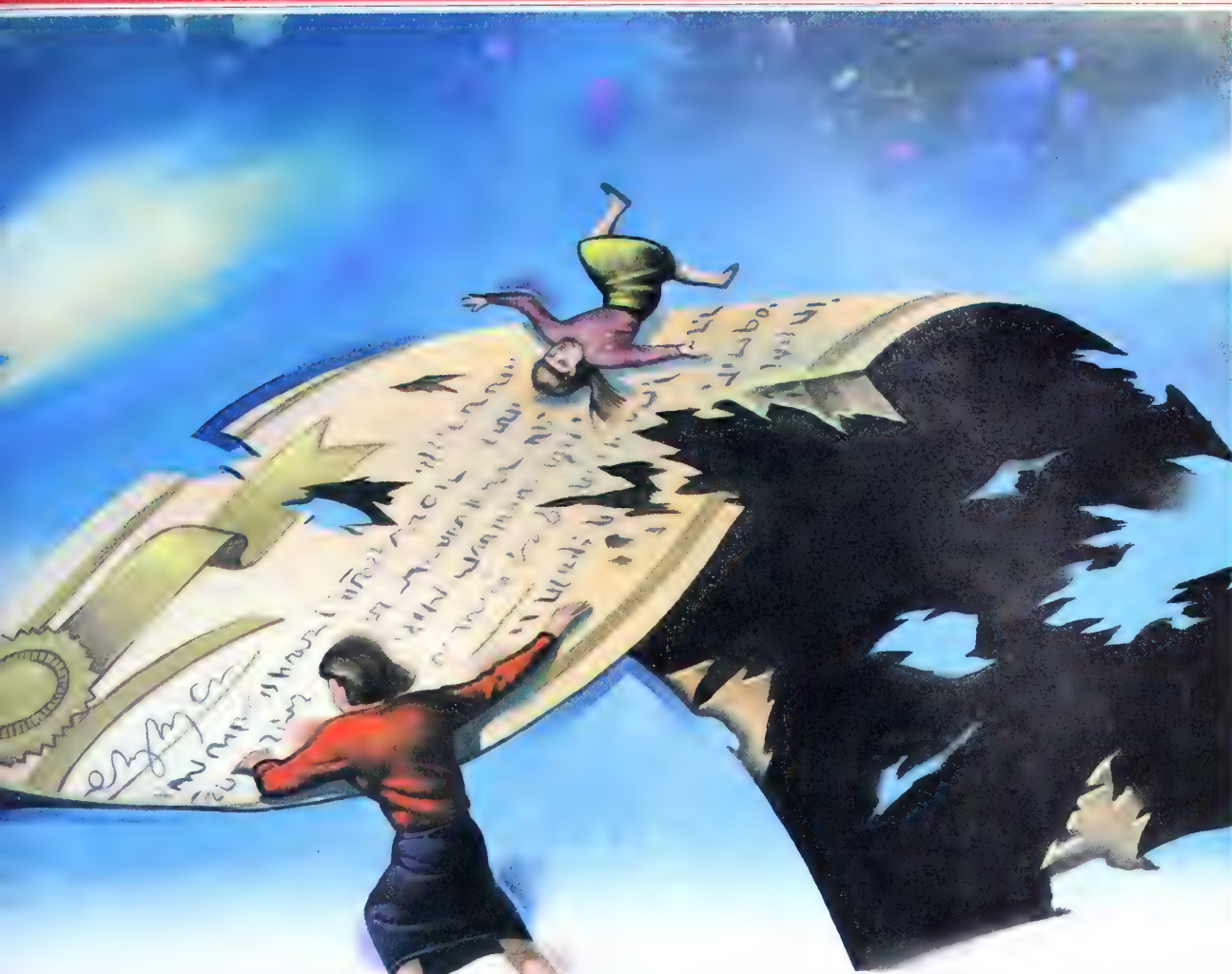
Amid all the worry and confusion, though, you actually can do much to safeguard your assets. Don't rush to cash out your policy or radically change your pension-fund investments. "Switching policies may be worthwhile for you, or maybe not," says Joseph M. Belth, an Indiana

University insurance professor who predicted many of the industry's woes.

So do your homework—lots of it. Yet the insurance industry is notoriously opaque, with its own bewildering lingo. But you can still learn a lot by questioning your insurer's financial strength with the major credit-rating agencies and state insurance regulators. Badger your insurance agent for answers about the stability of your insurers. Closely examine your employer's pension plan. Does your company make all your in-

vestment decisions for you, or are you a member of a defined-contribution plan such as a 401(k) that makes you decide how your pension money is invested? **BUM RAP?** Beyond that, your policy shouldn't be the core of your financial future but merely part of a well-diversified portfolio. If you have doubts about your policy, you'll need to know the paperwork.

**DON'T RUSH
TO CASH OUT YOUR
POLICY OR ALTER
YOUR RETIREMENT
PLAN. BUT DO
YOUR HOMEWORK—
LOTS OF IT**



ands, the financial penalties, and costs you might pay if you decide to e a change.

here will the next bad news come? Nobody knows, but few predict and to the failures. Right up until the yholder run, Mutual Benefit looked f it would muddle through. Still, e's no cause for panic. The industry ot about to collapse like the banks n the 1930s or the thrifts more re- y. Insurance has fewer fast-buck ts of the kind who plagued the sav- and loan associations with fraudu- schemes. Insurers generally remain ervative investors, with half their oluos in government or investment- e corporate bonds.

en in some of the bleakest corners insurance land, things are looking up. ch insurance giant Axa announced uly 18 a \$1 billion investment in the 3 American insurer, Equitable Life rance Society, whose bad invest- ts have kept it a perennial candidate he deep-six list. Axa says it scruti- d Equitable's investment portfolio, y item, and concluded that the t is over. "This is good news for

us," says Equita- ble CEO Richard H. Jenrette.

Executives at healthy insur- ers complain, with some justice, that they are being tarred unfairly. Consider John Hancock Mutual Life Insurance Co., one of six major companies down- graded on July 19 by Moody's Investors Service Inc. because of concern about heavy exposure to the ailing real estate market. Hancock, which went down two notches from the highest Moody's grade, has just 2.5% of its mortgages in de- fault, compared with 4.5% for all life companies. Insists Stephen L. Brown, Hancock's president: "We're not on some downward trend."

JERSEY JOLT. Ten years ago, the notion of the insurance industry in trouble would have been laughable. Insurers began the last decade as staid devotees of so-called whole-life policies, which showed steady, if unspectacular returns. For decades, everyone had grown fat following the lead of the large East Coast mutual-life companies. They focused more on the death benefits that

life policies furnish, not the investment aspect of the insurance: Life policies also are a tax-deferred savings vehicle that holders eventually can cash in.

But during the 1980s, mutual funds and other competitors emerged with re- turns that put whole life to shame. In- surers woke up and began offering a host of new products that promised siz- zling performance. And since the popula- tion was aging, insurers jumped into an- nuities with the same hell-for-leather philosophy. After the 1986 Tax Reform Act cut back on other tax shelters, annu- ity sales soared. And some insurers went too far and made promises they couldn't meet.

The Four Horsemen of the Insurance Apocalypse are junk bonds, commercial real estate, mortgage loans, and policy- holder runs. The last is a sinister phe- nomenon that removes any chance an insurer can survive the other three. Says analyst William D. Bitterli of Northing- ton Partners Inc., an insurance research firm: "Perception can drive insurance companies—which are based on faith— out of business."

Take Mutual Benefit. Its huge me-

nagerie of defaulted mortgage loans and empty office buildings was bad enough. Then, alarmed policyholders, including many pension funds guarding annuities and 401(k) plans, removed \$500 million. After Ruth Tell, a Passaic (N.J.) hospital employee, heard that credit-rating agencies had downgraded Mutual Benefit, she promptly surrendered her annuity with the insurer. Two weeks later, the company took its dive. Says Tell: "Right now, I feel pretty good about my decision."

The pain of an insurance collapse extends beyond the affected policyholder. Mutual Benefit backed some \$744 million in municipal bonds, and its takeover has sent the muni market into a tizzy. Within the insurance industry itself, the recent failures are rearranging the game board, with the strong preying on the weak. "Since Executive Life, there has been a distinct flight to quality," says James R. Hiner, principal at William M. Mercer Inc., an employee-benefits consulting firm.

SNORING WATCHDOGS. Trouble is, regulators don't have an inspiring record of flagging weak performers early and straightening them out. Los Angeles-based Executive Life was obviously in sorry shape for a long time, yet California officials did little to force a restructuring (page 46). Some states, such as New York, are tougher and more able than others. Unsurprisingly, those with weaker standards are more popular with insurers. Arizona, where only \$450,000 is needed to start an insurance company, has 150 staffers to watch 818 companies, while New York, where the minimum capitalization is \$3 million, has 360 people to regulate 368 insurers. In Louisiana, another weak-regulation state, former Insurance Commissioner Doug Green was sentenced to 25 years in federal prison for a variety of offenses he committed while in office, including money-laundering, mail fraud, and wire fraud. "If I were a man on the street, I wouldn't trust our state government to regulate the insurance industry," says Winston Riddick, executive assistant



INSURANCE EXPERT BELTH: BEWARE OF AGENTS WHO ARE MUM ON COMMISSIONS

to the Louisiana attorney general. The attorney general expects Green to appeal his sentence.

So it's up to you to look after your nest egg. Your insurer should pass a financial stress test. Look at its capital, defined in insurance-speak as "surplus," or net worth, plus the "mandatory secu-

rities valuation serve," which is aside to buoy tank investments. The rule of thumb is that a topflight company's capital should be 10% of assets. A second measure is Standard & Poor's Corp.'s turn on assets: 1985 through 1990, S&P rated companies above average if they earned at least a 10% ROA. The best advice may be to buy from large companies licensed nationwide and especially in New York. Be wary of a policy offering above-market yields: That's a sure sign of high risk.

The major rating agencies can do a lot of spadework for you. A.M. Best has been rating insurance companies the longest. Over the past several years, S&P, Moody's Investors Service Inc., Duff & Phelps, Weiss Research, and a handful of other companies have expanded their coverage of the industry.

The rating agencies are far from infallible. Glaringly, most failed to warn of the dangers at Executive Life and Mutual Benefit (page 46).

Still, many insurance analysts say there is some comfort in getting the ratings from several agencies. "I like a consensus among the rating agencies, and I like highly rated companies," says Glenn S. Daily, an independent insurance consultant based in New York. The agent you bought your insurance policy from—and paid a hefty commission to—can get the information for you. In Texas, the State Board of Insurance has an 800 number. Callers can find out if an insurer is licensed in Texas, how to file a complaint, and starting Sept. 1, a company's financial rating from the major service.

You can also trek to many local libraries to look up a company's rating, although the data there may be outdated. Better yet, call the rating agencies directly. Standard & Poor's will rate an insurer for free over the phone (212 208-1527), but it won't provide backup details. Others are more comprehensive, and you pay for the information. Best, for example, has a number that charges you \$2.50 per minute (900 420-0400). Weiss gives verbal reports on a company for \$15 over the phone (800

FIVE WAYS TO PROTECT YOURSELF

- 1** Watch the media for any bad news about your company's performance
- 2** Compare the ratings on your company from several major rating agencies. The higher the grades, and the more the different agencies agree, the better. Also check with your state insurance department
- 3** Ask your insurer or agent what paperwork you will need to complete, and what penalties you may incur, if you want to transfer your policy or annuity elsewhere. Check tax liabilities, too
- 4** If you're considering a transfer, search hard for an alternative. You could borrow against your current policy. But if you decide to switch, be wary of products with above-market yields
- 5** If you have money in a guaranteed investment contract in your employer-sponsored retirement plan, ask your employee-benefits office who is the GIC's issuer. You want to make sure your employer spreads the risk by investing with several different issuers. You may want to diversify your investments among other options such as stock, money-market, and bond funds

THE RATING GAME: WHEN A+ EQUALS C-

If you had called A.M. Best Co. on July 1 and asked for a rating on Mutual Benefit Life Insurance Co., you would have been soothed by the answer: A+. One week later, the venerable agency seemed only slightly less beat, rating the insurer "contingent"—Best's designation for sound companies with temporary troubles. But on July 16, there was no rating at all. Mutual Benefit had been seized by New Jersey's regulators.

What if you had rung up rival rater Weiss Research Inc.? The self-styled consumer-advocate agency showed a C ("fair") rating for Mutual Benefit as late as March, downgrading it to D+ ("weak") in June, and to E ("very weak") on July 12.

BETWEEN THE LINES. But don't confuse hindsight with 20-20 vision. Before you conclude that Best didn't live up to its name, remember that ratings are subjective. "These are opinions, not guarantees," says insurance industry watchdog Joseph Belth. The major agencies—Best, Standard & Poor's, Moody's, Duff & Phelps, and Weiss—use different approaches to the data they use. And their ratings have nuances that aren't immediately apparent. To help you sort out the symbols, BUSINESS WEEK has grouped them into seven levels and used these levels to

create a composite index (tables).

The 91-year-old Best is the most exhaustive of the raters, covering 3,800 companies. Its evaluations are based both on quantitative analyses of profitability, leverage, and liquidity and on qualitative study of companies' risk diversification, asset quality, and management. Best works closely with the insurers and takes a long-term view of their relationships with policyholders. It assumes the companies will survive several economic cycles over 20 years or more. That's one reason Best has a higher concentration of "superior" ratings than its competitors.

At the other end of the spectrum is Weiss, which started rating insurers in 1989. Weiss uses only public data—the statutory information insurers supply to state commissions—to compile its ratings, which follow a report-card format from A to F. Weiss examines whether a company's balance sheet would hold up in a severe recession, assuming that at least one is bound to occur during the life of a policy. So companies get far fewer "superior" ratings from Weiss than from Best.

In between these two extremes are the three specialists in hard-core financial analysis. S&P, Moody's, and Duff & Phelps have almost identical rating scales, whose similarity to bond grades

reflects their history as raters of debt issues and preferred stocks. They work in cooperation with the companies they cover, and their approaches are similar—though the three by no means move in lockstep. Thus, looking at their ratings may give the clearest comparison of opinion.

CLAMORING. Armed with this background, you're ready for the rating wars. Once you realize that a contingent A from Best is four notches below its highest mark, you'll see that the benign-sounding rating for Mutual Benefit was actually a red flag. And when you remember that the plethora of C's in Weiss's list describes a worst-case scenario, you can mentally adjust for the fact that the economy is emerging, however slowly, from recession.

Predictably, both Best and Weiss have come under fire as a result of the insurers' troubles: Best for being too kind and too slow, and Weiss for fueling policyholder panic. In fact, there's almost as much drama going on among the raters as there is among the insurers themselves. As consumers clamor for information about their insurers, it's likely that all five raters will fine-tune their methodologies—and that the consumer will be the winner. Until then, get as many opinions as you can.

By Joan Warner in New York

RATING THE 15 BIGGEST INSURERS...

Insurer ¹	A.M. Best	Moody's	Standard & Poor's	Duff & Phelps	Weiss	BW composite index ⁴
MUTUAL BENEFIT	A+	Aaa	AAA	NR ²	B	1.5
METROPOLITAN	A+	Aaa	AAA	AAA	A-	1.2
NETINA	A+	Aaa	AA+	NR	C+	1.7
WELLS FARGO	A-	A3	A	A	D	3.2
TEACHERS INS.	A+	Aaa	AAA	NR	B-	1.5
NEW YORK LIFE	A+	Aaa	AAA	NR	A	1.0
CONNECTICUT GENERAL	A+	Aaa	AAA	NR	C+	1.5
JOHN HANCOCK	A+	Aa2	AAA	NR	C	2.0
TRAVELERS	A+(c) ³	A2	A+	AA-	C	2.8
NORTHWESTERN	A+	Aaa	AAA	AA	A	1.2
PRINCIPAL	A+	Aa1	AAA	NR	B-	1.7
MASSACHUSETTS MUTUAL	A+	Aa1	AAA	NR	B	1.7
CINCINNATI NATIONAL	A+	Aa3	AA+	AAA	B+	1.6
MUTUAL OF NEW YORK	A+(c)	Baa1	AA-	AA-	C	2.8
NEW ENGLAND MUTUAL	A+(c)	Aa3	AA+	AA	C-	2.4

¹ Ranked by 1990 assets (2) NR = Not rated (3) (c) = Best's "contingency" rating, indicating it sees a temporary decline in profitability or liquidity (4) Average based on assigned value; the top rating is 1.0

...AND HOW TO READ THE ALPHABET SOUP

Description	A.M. Best	S&P/D&P	Moody's	Weiss	Assigned value*
Superior. Negligible risk	A+	AAA	Aaa	A+	1
Excellent. Small, slightly variable risk	A+(c) A, A(c) A-	AA+ AA AA-	Aa1 Aa2 Aa3	A A- B+	2
Good. High claims-paying ability for now	A-(c) B+ B+(c)	A+ A A-	A1 A2 A3	B B- C+	3
Adequate, but less protection against risk	B B(c) B-	BBB+ BBB BBB-	Baa1 Baa2 Baa3	C C- D+	4
Below average quality, higher risk factor	B-(c) C+ C+(c)	BB+ BB BB-	Ba1 Ba2 Ba3	D D- E+	5
Financially weak, high risk factor	C C(c) C-	B+ B B-	B1 B2 B3	E E- F	6
Nonviable, or about to be		CCC CC, D	Caa Ca, C	F	7

* Used to calculate BW composite index

DATA: A. M. BEST CO., STANDARD & POOR'S CORP., MOODY'S INVESTORS SERVICE INC., DUFF & PHELPS/MCM INVESTMENT RESEARCH CO., WEISS RESEARCH INC.

289-9222). The raters will mail you written analyses for a fee. For instance, Weiss sends out \$15 one-page company summaries or 18-page reports for \$45.

Sometimes, tracking your insurer is a simple matter of keeping up with the news. The wonder is not that some 1,100 of Executive Life's policyholders bailed out in the six weeks before the state takeover, it's that the rest did not. The company's woes had been very well publicized.

What if your research leaves you with no warm, comfy feeling about the safety

of your annuity or insurance policy? Should you surrender it? Alas, the answer is: It depends. You can change your policy and keep your tax deferral intact by filling out a 1035-exchange form with a new company. Your new insurer will make the transfer for you. But changing insurance or annuity policies can involve hefty surrender fees, new commission costs, and higher rates if your health has deteriorated. And if you die within two years of taking out a new policy, the insurer can investigate to see whether you misrepresented medi-

cal information when applying. Your beneficiaries could wind up with nothing. One option is to stay put with your insurer and borrow against the policy.

Remember, any agent has a financial interest in moving you to a new policy. As much as half of your first year's premium often pays a commission. "You should ask him about his interest in this," says Belth. "And he shouldn't hesitate to tell you."

It's not just owners of insurance and annuities who should put on their green eyeshades. So should employees with

WORSE THAN 'MY WORST NIGHTMARE'

For Katie Watson, it was adding insult to injury. Brain-damaged while in the hospital for pneumonia when she was 20 months old and still unable to walk or talk at age 11, the Phoenix girl relies on a \$1.4 million annuity from a malpractice judgment her parents won in 1986 to pay for her medicine, therapy, and home care. Unfortunately, that annuity came from Executive Life Insurance Co. of California, which was seized by state regulators in mid-April.

By May, Executive Life annuity payments were slashed 30%. Coming up \$3,500 short that month, Katie's parents, Vincent and Susan Watson, cut household spending to the bone and put their home on the market. They were afraid they might also have to halt Katie's therapy. "In my worst nightmare, I never thought this could happen," says Vince Watson.

HARDSHIP STATUS. The Watsons join more than 373,000 other Executive Life customers left in the lurch by the collapse of the junk-bond laden Los Angeles insurer. Some were there not by their own doing but because their employers had invested their pension money in Executive Life group annuities and guaranteed investment contracts (GICs). Many, however, sought out the company for the high yields its junk-bond holdings allowed it to pay. Now, they all face the harsh reality of having their future jeopardized by an unprecedented insurance debacle.

Dire as the Executive Life case is, it demonstrates that safety nets do exist. All insurance beneficiaries began receiving at least part of their regular payments after an 11-day halt in benefits following the seizure. Death benefits are being paid in full. And Executive Life customers facing a financial emergency can file for hardship status with the Cali-



KATIE WATSON AND PARENTS: EXECUTIVE LIFE'S DEBACLE THREATENED HER MEDICAL PAYMENTS

fornia Insurance Dept. to receive 100% of their monthly payment. Only the interest payments to holders of \$1.85 billion worth of municipal bonds, whose proceeds were invested in Executive Life GICs, have been stopped.

So far, 525 hardship requests have been granted, including the Watsons', whose full payments resumed in June. More often, other forms of rescue are emerging. Some companies, such as Pacific Lumber Co., are making up the shortfall in payments on annuities they purchased for pension plans. Pacific Lumber's decision came after pressure from employees and retirees. "I never in my wildest dreams thought I'd have to go to the front office in Scotia [Calif.] to picket and protest the loss of our pension," says Wiley J. Lacy, who retired from his job as a tax manager at Pacific Lumber in September, 1985.

Regulators, legislators, and those overseeing the insurer's conservator have also gotten an earful. "I'm not going to let anybody step on me. I want that money," says Olga P. Low, a 75-year-old Chicago widow with Executive Life annuity. She testified in Washington in mid-July at a congressional hearing about insurance failures. Like many Executive Life customers, she worries about what will happen in the long run. California regulators are negotiating the sale of Executive Life to a liquidation of assets that would leave with too little to pay customers. California funds in 49 states are supposed to cover losses if an insurer is declared insolvent, but some fear Executive Life's huge losses could swamp those funds.

None of the fixes will undo the damage Executive Life's victims have already suffered. "I'm telling my

participate in a company's 401(k) plan. About 65% of the money in such retirement programs is parked in GICs—usually called the “fixed-income fund” on the benefits statement. Superficially, a GIC resembles a certificate of deposit, but its principal value doesn't fluctuate and it pays a stated rate of interest. But unlike other pension plans, GICs aren't fully insured: The money often is as good as the credit of the insurance company. “All of a sudden, people are coming to grips with the fact that a guarantee by an insurance company isn't really a guarantee,” says Hiner. “It's like a light just went on.”

Others: “Find out what your bank insurance company are doing,” says Revlon, who invested her nest egg in Executive Life annuity six years ago. “I thought insurance companies were safe. I had no idea about junk bonds.” But, of course, is that Executive Life's problem? It's downgraded from most rating agencies in early 1990, when junk-bond losses were taking their toll. Thousands of Executive Life customers then cashed out their annuities, but some annuity beneficiaries were trapped by the terms of the contracts. Eli Schefer, 71, a retired mechanical engineer, spent months deconstructing Revlon and Executive Life annuities. His pension, part of a group annuity Revlon bought in 1986. “They told me I was locked in,” says Schefer, who helplessly as the insurer collapsed. **BLOW.** Others heard of Executive Life's troubles but trusted that government guarantees of insurers would keep their investments safe. “We were all supposed to be protected by the regulators,” says a New York businessman who in 1987 bought mutual funds backed by Executive Life annuities. He was incensed to learn now that the annuities were guaranteed only by the insurance company. In divvying up the money available to bondholders must wait to be paid. Executive Life's insurance customer investor fears he may wind up with a fraction of the money he put in. “It's a terrible blow to me.” The victims are also calling for reforms to prevent future debacles. “It's about time the federal government stepped in and put some very strong controls on the insurance industry,” says Mellvine Fuchs, 71, an Executive Life shareholder in Balboa, Calif. “I simply want to put the insurance company out of business.” “Katie has suffered from this,” says Susan Watson. The judge who ruled that Executive Life assured the Watsons their daughter's financial needs were met. But just in case things don't work out, their house is still for sale. Confronted with the roller coaster they've been riding, caution may be well advised.

By Kathleen Kerwin in Los Angeles

Or a bomb that went off. Executive Life's California unit, for example, sold about \$3 billion in GICs that are now practically worthless. Employees of Honeywell Inc. invested in \$72 million worth of Executive Life GICs. At Unisys Corp., it was \$134 million, and at Ralston Purina Co., \$14 million.

When Executive Life fell, the fate of the GIC-subscribing employees was in their employers' hands. Ralston Purina made its employees' investments whole—but made it clear it was under no legal obligation to do so. Georgia-Pacific Corp., after getting speedy approval from the Labor Dept., substituted another carrier's GICs for its employees' Executive Life GICs—and it became a claimant on the insolvent insurer. Unfortunately for their employees, Honeywell and Unisys aren't paying. Unisys argues that it shouldn't do anything because defined-contribution plans put the risk squarely on the participant, not the employer. “Whether it's in these insurance annuities or Unisys stock, or anybody's stock, it's an investment, and investments unfortunately can go up or down,” says Unisys spokesman Mark S. Lipscomb. “There is no absolute guarantee.” Honeywell won't comment.

Of course, policyholders in such a jam can exercise the great American right to sue, as have disgruntled employees at Honeywell and Unisys. And they can raise such a stink that the government gets involved on their side. That's what employees at Pacific Lumber Co. did after Houston financier Charles E. Hurwitz's Maxxam Group Inc. acquired their company, used the excess money in their pension plan to pay down debt, and converted the remaining retirement funds to Executive Life annuities. Although the workers' suit is far from resolved, it helped spark congressional hearings. And the Labor Dept. weighed in by suing Maxxam and Pacific Lumber, too. Pacific Lumber has now agreed to make its Executive Life annuity holders whole. Pacific Lumber President John A. Campbell denies that the company's offer was a response to pressure.

IN LIMBO. Employee-benefit consultants advise checking out the creditworthiness of GIC carriers. Find out whether the GIC portfolio is diversified among several carriers or just one. If you are at all concerned, opt for a more diversified portfolio in your 401(k) plan, perhaps including stock, money market, or bond funds. Employers have to offer you more 401(k) choices than just the GIC.

What happens if you're a policyholder in a company seized by regulators? You live in a netherworld. “How long will we be stuck here?” grumbles Ronald G. Elias, comptroller of Cleveland's Empire Plow Co., a small farm-equipment maker whose \$350,000 in retirement funds is

TERMS OF THE TRADE

ANNUITY In return for a lump-sum investment or regular premium payments, annuities pay income at fixed intervals for a set number of years in the future or for life. *Fixed annuities* reset interest rates periodically and offer steady growth. *Variable annuities* invest premiums in stocks, bonds, or other assets, making your payout dependent on portfolio performance.

Immediate contracts are bought with a lump sum and provide income soon after you buy the annuity. *Deferred annuities* are bought far in advance of retirement, and premium payments accumulate tax-free.

DEFINED-BENEFIT PLAN Pension plan that pays retirees a fixed income based on years of service and salary. Participants make no investment decisions. Employers are obligated to fund the plan to pay projected benefits.

DEFINED-CONTRIBUTION PLAN Retirement plan, to which employees often contribute, that gives participants an active role in managing their money. Return is based on how well the chosen investments do. The category includes 401(k) savings, profit sharing, and employee stock ownership (ESOP) plans.

GUARANTEED INVESTMENT CONTRACT

A popular investment option in 401(k) plans, GICs are contracts between an employer and an insurance company. They pay a fixed rate of return for a set number of years, after which capital is returned or the GIC renewed.

TERM LIFE Life insurance that pays a death benefit if the policyholder dies within a specified period of time. With standard *increasing term* policies, the premiums rise greatly with age, while the face value remains the same. *Decreasing term* policies keep the premium constant but decrease the face value.

WHOLE LIFE These policies have a fixed premium. Any excess over the amount needed to cover the death benefit is channeled into a savings or investment account that grows tax-deferred. *Variable life* policies also have fixed premiums but put the cash value in a separate account that you allocate among various mutual funds. *Universal life* allows you to alter premium payments by amount or time period, so you can change the level of the death benefit or cash value.

frozen inside state-controlled Mutual Benefit. Only annuity payments and death benefits are permitted for Mutual Benefit customers. But they can't transfer their policies or borrow against them. Mutual Benefit holders are faring better than their counterparts at Executive Life's California subsidiary, though, where monthly annuity checks were cut 30%.

As frustrated as policyholders of seized companies may be, most experts recommend keeping up on premium payments. If you skip payments, many policies include a provision that automatically "borrows" the premium money against your policy's cash value. After a while, there is nothing left to borrow against, and the policy is no longer in force. "Keep the policy up to date," says Kevin

E. Foley, deputy superintendent of the New York State Insurance Dept., who is operating Executive Life's New York subsidiary. "It's just crazy not to."

HARDSHIP REQUESTS. In hardship cases, such as medical emergencies and imminent homelessness, regulators may approve policy cash-outs. But it's not a snap. College costs don't cut it. Executive Life of New York, seized last April by regulators, has had 288 hardship requests since then. Money has been paid out to policyholders in dire straits in some 90 cases, while 102 requests have been rejected, 82 have been returned for more information, and 14 are still under consideration.

Everything may yet work out in the end. The regulators hope to keep the seized companies going, perhaps to sell them to more robust insurers. For instance, Monarch Life Insurance Co. already has attracted several suitors, since most of its bad assets are sitting in a separate holding company. Prospects for the other insurers are dicier, however, because they still have a lot of rotten investments backing up the policies. Whatever ensues, don't expect speed. The largest life company failure



NEW YORK DEPUTY INSURANCE CHIEF FOLEY: DON'T SKIP PREMIUM PAYMENTS

until this year—\$3.4 billion Baldwin-United Corp. in 1983—was a slow-motion rehabilitation. Baldwin languished in state hands for more than a year before Metropolitan Life Insurance Co. took over its 165,000 annuity policies.

The worst case confronts those souls whose only hope lies in state guaranty funds—which may not guarantee everything. The funds are fed by solvent insurers who pony up to pay off policyholders. But the coverage is a dismaying patchwork. Whether you will get all your money depends on where you live. California covers only 80% of a policy, a mere 20 states cover GICs, and annuity coverage varies widely. Louisiana and Washington, D.C., don't even have life insurance guaranty funds.

Given all the turmoil, some hopeful trends are on the horizon. Expect to see tighter regulation in the next two years or so. Washington is making increasingly serious noises about imposing federal standards on insurance, which by law is now a state concern. Already, Capitol Hill scrutiny has forced state regulators to write their own national code, unifying and beefing up standards. If state

legislatures don't act, other states will not cooperate with the regulators.

The feds might extend their purview to annuities. Senator Howard M. Metzenbaum (D-Oh.) wants to propel a reluctant U.S. Pension Guaranty Corp. into protecting these insurers provided retirement products. The agency's job is to cover pension plans when strapped employers can no longer pay promised benefits. "The PBGC claims it has no money if an employer terminates a pension plan and buys annuities for workers," says Metzenbaum. "The PBGC should be protecting the retiree."

It's heartening that some employers are taking a hard-eyed interest in how retirement money is invested. Last April, Chicago-based FMC Corp.

instituted more stringent standards for its GIC investments in the manufacturer's 401(k) plan: No more than 15% of the GIC option may be invested with any one insurer. More recently, about 50 big corporate buyers of the Executive Life annuities formed an alliance to try to get their employees' money back.

Another plus: Like banks, insurers are consolidating, which presumably will make them stronger. Right now, the U.S. has 2,300 life insurance providers. "That's far too many," says Ardiand chairman of Gill & Roeser Inc., a firm that advises insurance companies. By the end of the decade, there will be a third fewer." Phoenix Mutual Life Insurance Co. and Home Life Insurance Co. have opened talks about a union that would boost their capital and create one of the nation's largest insurance producers, with \$10 billion in assets.

Meanwhile, insurance remains a vexing question for people who always took their coverage and investments for granted. Perhaps it's for the best that the spotlight now is shining on this long-observed stanchion of America's financial well-being. The structural cracks are too serious to overlook.

By Larry Light and Christopher Farley with Michele Galen and Suzanne Wood in New York, Lisa Driscoll in New Hampshire, Susan Garland in Washington, and bureau reports

THE TOP ISSUERS OF GUARANTEED INVESTMENT CONTRACTS

Company	Total GICs Millions of dollars
PRUDENTIAL	\$21,785
METROPOLITAN	18,265
AETNA	12,585
JOHN HANCOCK	9,648
TRAVELERS	8,444

DATA: CONNING & CO

DO MORE BABIES MEAN FEWER WORKING WOMEN?

As fertility rates rise, the U.S. may be facing a new labor shortage

Like the majority of women nowadays, Ann McPherson joined the labor force after she graduated from college. That was in 1980. She held several jobs, most recently as office manager at a small company in Denver, Martinetta Corp., where her husband is a financial analyst. But McPherson, 33, went part-time after her son Drew was born in 1988, then quit entirely after he arrived this year. "If women try to do it all, the children suffer," she says. "I'll go back to work maybe in 10 years, after we have a third child."

Women like McPherson are at the core of a new and raging debate. For the first time in decades, women are having more children. At the same time, the number of women in the labor force has slowed. The debate is over whether the two trends mean the labor force is shrinking or whether they are linked.

Susan Heyward, a service-president at Yankelovich Clancy Shulman, which surveys American attitudes on basic values, the link is unbreakable. "Women are adding," she says, "that they want to shift the amount of time they put into their careers." To others, though, the slowing trends are a statistical quirk, exaggerated by a perception that has put women out of work. "We haven't had anything to prove that women are staying home," declares Heidi Hartmann, director of the Institute for Women's Policy Research in Washington, D.C.

WAGES? A lot is riding on who turns out to be right. Many economists have expected the labor shortages of the 1980s to resume after the recession. But it's already clear that "labor shortages in the 1990s will be different than in the 1980s," says Howard Gordon, an economist at the Bureau of Labor Statistics

who is revising his estimate of how many women will enter the job market through the year 2000. If women stay home in droves, the shortages could be worse than expected. That could drive up wages and make employers scramble to hold down costs or boost productivity.

All of this may depend in part on what's really happening to the so-called fertility rate, which measures the average number of children women have. After hitting 3.7 in 1957, the height of the baby boom, the figure sank like a stone, bottoming out at about 1.8 in the mid-

1970s. But recently it has started to rise again. By last year, women of childbearing age had an average of 2.1 kids each, the number at which the population grows instead of shrinks.

Those who think this is just a blip point to differences between generations. Women in their 30s, who put off having children until their careers were on track, are now having children before it's too late. At the same time, some women are having kids earlier, in their 20s. The result could be a "bunching" effect that's driving up the fertility rate. "What's happening is overlapping cohorts having kids simultaneously," says Thomas J. Espenshade, a sociology professor at Princeton University.

Others see this explanation as too pat. Carl Haub, a demographer at the Population Reference Bureau, a private research group in Washington, says that by 1988 fertility rates had begun to rise for women of all ages. Most significantly, births to white 15-to-17-year-olds, which had been flat for years, jumped

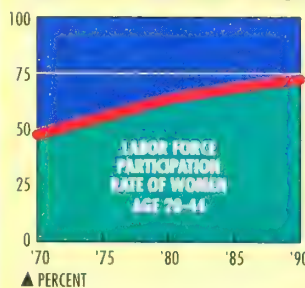
by 9% between 1986 and 1988. "This could have a tremendous long-term impact on the fertility rate," says Stephanie Ventura, a demographer at the National Center for Health Statistics, the government agency that tracks fertility. "If you start childbearing that early, you're likely to have more kids, regardless of what you say now."

JOB DROUGHT. Would this be enough to keep women at home? The increase in working women has slowed for sure: The labor force participation rate of women age 20 to 44 jumped by 8 percentage points between 1975 and 1980, by 5 points over the next five years, and by 3 points from 1985 to 1990 (charts). The rate didn't budge at all from 1989 to 1990—which hadn't happened in two decades. Hartmann and other economists mostly blame the recession. They note that jobs in retailing and services, where many women work, started to dry up even before the recession began. For proof, they point to the welfare rolls, which many single mothers join if they're jobless. A record 4.3 million families are on welfare now, up 13% since 1989.

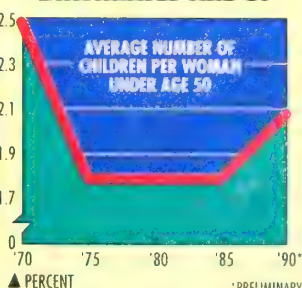
In fact, many analysts still believe that the upper limit of women who want to work is



WOMEN ARE TAKING JOBS AT A SLOWER PACE...



...MAYBE BECAUSE BIRTHRATES ARE UP



close to the 90% found in Sweden. Some 75% of American women age 25 to 54 work outside the home. So if the theory is right, their participation rate may rise again as more jobs open up, since most families need the money women earn. "I don't see men's earnings shooting up to compensate for women dropping out," says Howard V. Hayghe, a BLS economist who studies women's issues.

What makes the analysis tricky is the anecdotal evidence of a shift in national priorities back toward families and children. Yankelovich's annual survey asks whether people would quit work permanently if money allowed. For years, about a third of all women said yes. Then in 1990, the figure hit 56%. That year, 39% of women said women should work only part-time if they have children in school, up from 31% in 1989. Other surveys, by the Roper Organization and *The Washington Post*, have found similar changes in opinion. "Women have more of an interest in staying home with their kids, even though we expect to return to a job later," says Heidi L. Brennan, the co-director of Mothers at Home, a support group based in Washington. Its nationwide membership has doubled in two years, to 15,000.

GENDER GAP. If Brennan is right, employers could face tough times. Most companies are bracing for the labor and skill shortages predicted in 1987 by the Labor Dept.'s *Workforce 2000* study. And even those projections may be too optimistic. When Fullerton updated the BLS figures two years ago, he estimated that 12 million women would join the labor force between 1988 and 2000. Now he's rethinking this. If only 10 million more women choose to work, it would cut 10% off the overall labor force increase of 19.5 million men and women that Fullerton had predicted. This might be offset somewhat by last year's immigration law, which may let in more than a million new workers over the next decade. Still, says Fullerton, hiring could "be difficult for employers looking for people whose native tongue is English."

Paradoxically, some economists believe that living standards could rise if fewer women take jobs. In this view, in the 1980s employers chose relatively cheap labor as an alternative to improving productivity. Labor shortages should finally make them boost output per worker—and then pay everyone more, says Richard Jackson, a research fellow at the Hudson Institute, which helped produce the *Workforce 2000* study.

The idea that fewer workers could lift overall U.S. income sounds daft. But then, a couple of years ago, hardly anyone saw even a chance that women might have second thoughts about working away from home.

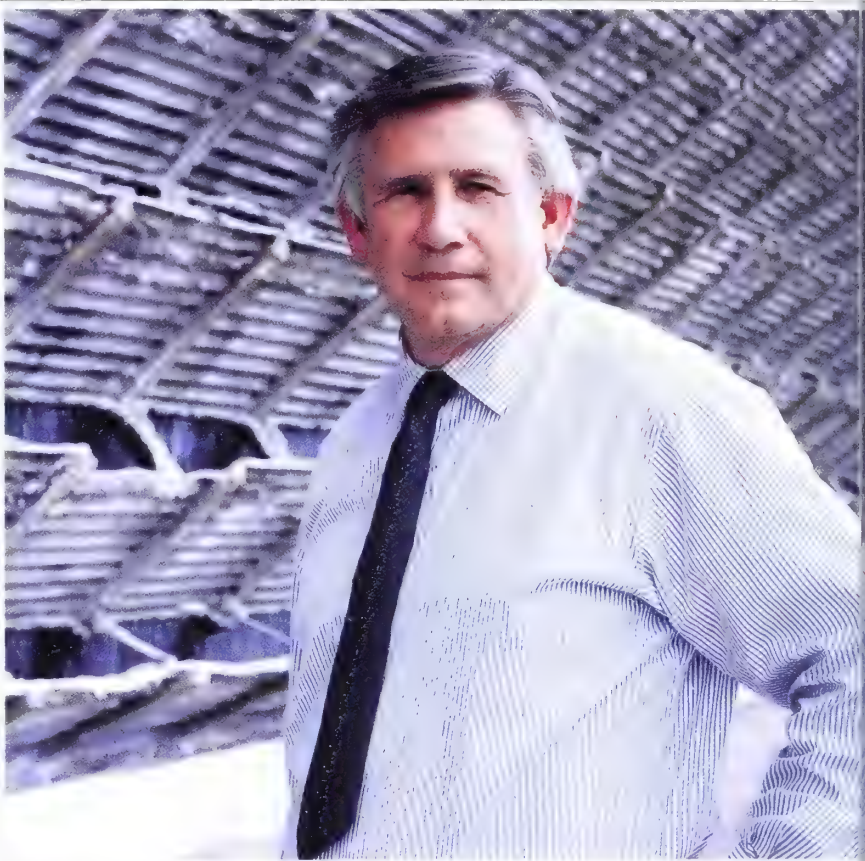
By Aaron Bernstein in New York

The Corporation

STRATEGIES

HIGH NOON AT TUCSON ELECTRIC

With investors pushing for bankruptcy, the utility has few options



The news came over a pay phone at Los Angeles International Airport on July 16—and it wasn't good. Tucson Electric Power Co.'s general counsel, Dennis R. Nelson, along with other executives, had just come winging in from Tucson to meet with the utility's bankers at the L.A. Hilton. But the meeting was not to be. After checking in for messages, Nelson was informed that five of the utility's big creditors had just filed a petition to push the debt-deluged utility into bankruptcy. As Nelson hung up, it looked as if a seven-month-long high-wire act to keep the ailing utility upright had just crashed.

Now, the stage is set for what could become the largest utility-company

CEO Bayless:
A frantic,
seven-month
survival fight

bankruptcy in U.S. history. Even if Tucson manages to tie the noose this time—and that's unlikely—it will require a massive restructuring. That will be quite a jolt to Tucson's investors, creditors—and Arizona ratepayers. Already, some

Corporate America's biggest names—Ford, IBM, and Philip Morris—have millions thanks to this little-known utility tucked away in the Arizona desert.

Not that Tucson executives have tried to avoid this predicament: They have alternately cajoled and arm-twisted lenders and vendors. They have pleaded their case before defiant state regulators. "This turned out to be one of the most complex workouts that was probably ever attempted," says Tucson Electric

resident and Chief Executive Officer Charles E. Bayless, who came on year to save the company. "We always walking on a tightrope." rope may have finally snapped. started to fray in 1985, when Tucson Electric, like other newly deregulated utilities, sought growth in bold diversification moves. Then-CEO Einar Greve, engineer, spent \$350 million on acquisitions that took the utility into new areas such as banking, car leasing, and real estate in Phoenix. But a plan to expand Tucson's core business fell through, thanks to an aborted merger with San Diego Gas & Electric in 1988. Greve's investments started to sour in the late 1980s and eventually cost the company \$83 million in losses during 1989 and 1990. By the end of 1990, the company labored under a staggering \$2 billion debt load—or 90% of total capital. Cash had dwindled to just \$3.7 million by the end of 1990, from \$21.5 million in 1989. Tucson posted a \$387 million loss in 1990—on \$499 million in sales.

SHED IMAGE. A whiff of scandal also surrounded the utility. In 1989, the Securities & Exchange Commission launched an insider-trading probe into Tucson. Greve had sold \$1 million worth of stock just before Tucson's ills became public. Greve also drew harsh publicity in 1989, at 61, he married a 25-year-old former topless dancer. The SEC investigation, still ongoing, cost Greve his job in 1989, when Tucson's board gave him the heave-ho. Greve is cooperating with the feds and denies the charges, according to his lawyer, Theodore Sonde. To this quagmire stepped Charles Bayless, a onetime power-line worker and former chief financial officer of the Public Service Company of New Hampshire—a utility that emerged from bankruptcy court itself in May. Since taking over as CEO last year, the burly Bayless worked to clean up Tucson's sooty image by courting investors and the courts. He also hired L. A. bankruptcy lawyer Richard B. Levin to orchestrate a complex legal strategy.

Last year, Tucson took a cataclysmic turn for a utility: It omitted its dividend. Even that didn't conserve enough cash to cover the company's debt service. By early this year, more than \$70 million in bank lines were coming due, but the company couldn't pay, raising the specter of bankruptcy—and a new era. Should the utility be forced to renegotiate its more than \$650 million in power bonds—issued for power plant construction—future tax-exempt issues would be off-limits. And they are the financial lifeblood of any utility.

In January, Bayless called some 60 creditors to the Doubletree Hotel in Tucson. There, he delivered the bad news: The company was declaring a moratori-

um on debt payments and other bills. Says one Los Angeles banker, whose bank holds about \$75 million of Tucson Electric debt: "We all knew about the company's problems, but it still hit hard."

Three months later, Tucson handed out its restructuring plan. By then, the utility had suspended nearly \$200 million in various payments to its banks, vendors, and other creditors. With unpaid interest being added to the principal on this \$200 million, Tucson's \$5 million in monthly suspended-debt payments had escalated to \$7 million.

The company's 40-page plan contained more than a few bombshells. The utility's 46 banks, holding more than \$1 billion in various pieces of debt, were asked to extend maturity dates on lines of credit and revolving funds. Interest rates, some as high as 12.2%, were to be slashed. Coal contracts were to be renegotiated, with prices cut by as much as 25%.

NEW FORECAST. The real linchpin, though, was getting a rate boost from the regulators, namely the Arizona Corporation Commission (ACC). What was needed? A 10.5% hike in rates for the coming year that would generate \$51 million annually starting on June 1.

Shuttling between Los Angeles, New York, and Tucson, Chief Financial Officer Ira R. Adler began talks with the banks and other lenders. But the bankers were skeptical and hired Price Waterhouse to work up its own revenue forecasts for Tucson. These were more gloomy.

The ACC also questioned Tucson's numbers, rejecting 25% of the \$706 million in costs for building a plant that came on-line last June—costs the utility hoped to recover. Then, the ACC cut Tucson's 10.5% rate request to 4.5%. That meant it would get \$20 million in added yearly revenue, not \$51 million. Says ACC

THE TRAVAILS OF TUCSON ELECTRIC

1985 Executive Vice-President Einar Greve, an engineer by training, is named chief executive

1986 Greve diversifies beyond the utility business, investing more than \$350 million in real estate, car leasing, and other businesses

1988 With investments souring and unused capacity dragging down earnings, Tucson fails to pull off merger with San Diego Gas & Electric

1989 Tucson's board of directors fires Greve, who is the target of an insider-trading investigation by the Securities & Exchange Commission. Company posts first loss in more than 20 years

1990 Tucson hires Charles Bayless as chief financial officer from bankrupt Public Service of New Hampshire. Six months later, he becomes CEO. Tucson shocks investors by omitting dividend

JANUARY, 1991 With its cash dwindling and \$70 million in bank debt coming due, Tucson asks creditors and lenders to accept moratorium on payments

MARCH, 1991 Utility proposes dramatic restructuring plan, asking creditors to re-write contracts and lenders to accept reduced payments. Company subsequently amends plan to substitute 60% of utility's common stock for much of its debt

JULY 16, 1991 Ford, Philip Morris, IBM, and other creditors petition the U.S. Bankruptcy Court in Phoenix to force Tucson into involuntary bankruptcy

DATA: BW

Utilities Div. Staff Director Gary Yaquinto: "We told them, 'We're not going to save you guys at the expense of our ratepayers.'"

Ford Motor Credit Co. also dug in its heels. Back in the mid-1980s, Tucson sold off several power plants to corporate investors such as IBM, Ford, and Philip Morris. It then paid them a lease roughly equal to the mortgage payments due on the plant assets. But any appreciation on the property would go to the investor-owners. Ford's credit unit had invested \$38 million to be part owner of the company's Irvington power plant, but Bayless wanted to suspend lease payments.

When Tucson withheld funds starting in February, Ford had to fork over nearly \$3 million in mortgage payments to Morgan Guaranty Trust Co. without collecting offsetting lease payments from the utility. Tucson refused to reimburse the auto maker. Ford Credit filed a lawsuit in state court in mid-April demanding the money. Ford hasn't commented on the matter.

Tucson managed to get Ford's claim thrown out of state court, arguing that the company's banks, not Ford, were the real creditors. Even so, Tucson faced objections from other investors, including IBM Credit Financing Corp. and Philip Morris Capital Corp. Tucson re-

vised its restructuring plan to offer 60% of its stock in exchange for much of its debt. But it was too late. By mid-July, though talks were continuing with other creditors, the investor-owners petitioned the court to place Tucson into involuntary bankruptcy.

Will Tucson wiggle free? Perhaps. The utility is pressing the petitioners to drop the suit. But given the depths of its woes, it looks as if the lights are still flickering at Tucson.

By Ronald Grover in Tucson, Ariz.

FUQUA RUNS INTO A PATCH OF TALL WEEDS

Its Snapper mowers are coughing—as are Qualex labs

If only selling lawn mowers were as easy as giving them away. During Fuqua Industries Inc.'s annual meeting in June, Chief Executive Officer Charles R. "Red" Scott wanted to soothe stockholders, who had watched their shares slip from 32 to 12 over the past three years. So, Scott held a raffle: One lucky soul walked off with a 21-inch Snapper mower.

He may have been the only happy shareholder that day. Battered by recession, high costs, and fierce competition, Fuqua's Snapper unit is in a slump. Its other main business, Qualex Inc. photo finishing, is also under fire from rivals. Fuqua owns several sporting-goods businesses, too, but its two core units account for 88% of revenues. In short, Fuqua is ailing. This year, it posted a \$15 million loss on \$211 million in sales during its first quarter. And it's expected to lose about \$17 million by yearend on \$890 million in revenues, reckons Shearson Lehman Brothers Inc.

FRESHLY SEEDS. Although he has been CEO at the company for just six months, Scott is no stranger to Fuqua's woes. He served as chairman of Intermark Inc., a holding company in La Jolla, Calif. Back in 1983, Intermark acquired Fuqua's controlling interest in Pier 1 Imports Inc., the home-furnishings retailer it has since sold.

In 1989, founder J. B. Fuqua sold his 6.6% stake in Fuqua to Intermark for \$38 a share—a \$6 premium at the time but below Fuqua's \$45-a-share break-up value. That, added to earlier buys, left Intermark, which also owns the Western Sizzlin' Inc. restaurant chain and several real estate companies, with a 27% holding. But Fuqua's profits fell (chart)—scuttling Intermark's plans to amass 51% and beating down its stock 90% since January, 1990.

With his investment in distress, Scott persuaded Fuqua's board of directors in February to let him take over as CEO,

replacing Lawrence P. Klamon, who left in June. Says Scott: "I finally realized it was time to take drastic action." Decisiveness may be in Scott's blood: He's the grandnephew of General George S. Patton. Already, Scott has cut the corporate staff from 41 to 18 people and brought in new top management at Qualex.

His biggest challenge: refashioning Snapper, the nation's No. 2 lawn-mower manufacturer behind Toro Co. Its riding and walk-behind mowers, sold only by authorized dealers, are first-rate—and priced that way. They start at \$189 and run up to \$6,000. But rivals have flooded

Wal-Mart Stores Inc. and other discounters with private-label brands that cost little as \$89.

These competitive pressures are creaming Snapper, which lost \$300,000 last year on \$238 million in revenue. And Snapper lawn mowers have been piling up in storage, sending inventory

costs soaring. Snapper's main assembly plant is currently running only 20% of capacity. Dry weather and housing downturn have clipped everyone. "Snapper was much slower to react to the backed-up inventory," says Dennis P. Himel, treasurer at Toro.

To lower Snapper's pricing, Scott is slashing costs. Snapper's plant

will soon be cut from three to one, while product redesigns will reduce parts, manufacturing costs, and suppliers. On the marketing front, there's a new national ad campaign starring the jaunty psychiatrist character from the TV show *Cheers*. Snapper may roll out cheap mowers under a new name.

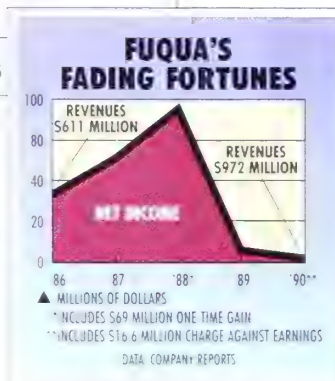
Meantime, Scott wants to improve the fuzzy picture at Fuqua's 51%-owned photo-finishing business. Qualex offers overnight developing service for film dropped off at retail outlets and boasts a leading 20% market share. But demand is being pinched by the downturn in travel and the popularity of camcorders.

The company tried to maintain profitability by hiking prices last year, but regional competitors undercut it, and Qualex retreated. One-hor "minilabs" are also battering Qualex. That's why sales dipped about 1%, to \$624 million, in 1990, while operating income was flat at \$44 million.

Qualex's new automated photo-finishing "microlabs" may help when they're rolled out a few stores later this year. Customers insert their film in these machines and return in 10 minutes to pick up the developed snapshots. Though speedy, the service will be expensive—about three times the \$7-a-roll for overnight service.

Scott promises "to make the company work for the shareholder again." He'd better: Rivals will keep investors amused for only so long.

By Walecia Konrad in Atlanta



BY ANDREA ROTHMAN

MARGARET JORDAN: NURSING HMO BACK TO HEALTH



Margaret H. Jordan is one of those people who can't stand to watch something done wrong. Early in her career, the nurse was working in a San Francisco hospital on a health care program for the poor. It drove her nuts to see how ill-coordinated the program was: Funds were allocated sloppily, and the poor didn't get nearly the services they deserved. "As a result," she says, "I knew I wanted to coordinate."

Jordan, 48, has spent nearly a quarter of a century coordinating—and improving. She is vice-president and regional manager of Kaiser Foundation Health Plan of Texas, a health maintenance organization. Jordan took the job in 1986, when the unit of Kaiser Permanente was losing money and membership. Jordan added four locations, bringing the total to 10. She recruited 115 doctors to add to the staff of 35, made the unit more competitive, and phased in strict cost controls. Membership has soared more than 130%, to nearly 118,000. Losing \$6 million in 1986, the HMO is expected to break this year and make a profit within 12 to 18 months. Jordan was Georgetown University's first black nursing graduate in 1964. She joined Kaiser in 1981 to help run an Atlanta HMO. Now, the tennis-playing administrator is to assume "a much more visionary role." For example, she wants to tailor preventive medicine programs to different ethnic groups. Whatever she does, it will be a lot easier now that the HMO's foundation is healthy.

By Stephanie Anderson Forest in Dallas

JEFFREY WALSH: WHEN THE BIG DOLLAR IS ON MONA LISA'S NOSE . . .

Jeffrey Walsh was an entrepreneur before he could pronounce the word. At 6, he recalls selling matches to other kids. By 12, he procured issues of *Playboy* and would sell the pages out and sell them to neighbor kids. Walsh was 13, he was in the police in Ossining, New York, even traced a big business to his father—but they let him off with a stern warning to his mother and father.



Older now, but no less ambitious. Through his Bronx-N.Y.-based Walsh Enterprises, the 24-year-old entrepreneur peddles ArtWatches—wristwatches with detail from famous paintings on the faces. Walsh's earliest timepieces, back when

he launched the business in 1989, featured works by the masters, including van Gogh, Monet, and Picasso. He has since added new images, such as wild animals in Africa by environmentalist painter Betsey Burhans Fowler.

Walsh got the idea for his business from a joke he heard while an undergraduate at the University of Pennsylvania's Wharton School: "What did Mickey Mouse get for his 60th birthday? A Dan Quayle watch." He found a watchmaker to add Quayle's face and sold 1,500 watches at \$50 apiece. Later, recognizing the popularity of Impressionist painting reproductions in dormitory rooms, he hatched the ArtWatch idea and made it his senior thesis.

Walsh sold 100,000 watches last year and expects to sell 275,000 worldwide in 1991. The watches, which retail for around \$50, are available in department stores, museum stores, and catalogs. Realizing that their popularity will likely peak one day, he's already planning other businesses, including a line of sports-related items. But, he says, "I can't tell any more about it." Now, Geoffrey, it wouldn't have anything to do with fireworks, would it?

JEFFREY MONTGOMERY: RAISING CASPER THE GHOST FROM THE DEAD

Every year, as his family made its annual camper trip up the Pacific Coast, Jeffrey A. Montgomery would bury his face in comic books. "What else was a kid going to do on a ride from Los Angeles to Oregon?" he asks. Now 27, he's still into comics, as chairman of Harvey Comics Entertainment. But this isn't child's play. "I look at myself as a character manager," he explains.



Montgomery is hustling to resurrect a galaxy of characters including Casper the Friendly Ghost, Richie Rich, and Baby Huey. When he bought Harvey for \$8 million in 1989, it was producing only two comics a month, and its characters hadn't been on TV in years. He dug into the archives for old comic books to rerelease, first sprucing them up with modern language and fresh color. He now has 15 monthly titles, including the newly acquired *New Kids on the Block*.

The comics are intended to whet readers' appetites for bigger things. This fall, Harvey will begin syndicating 65 episodes of "color-upgraded" *Casper & Friends* TV shows. Warner Brothers is planning a Richie Rich movie with *Home Alone*'s Macaulay Culkin. MCA Inc., which paid \$3 million for 20% of Harvey last year, has asked Steven Spielberg's production company for a Casper movie and a Baby Huey short. Harvey characters may show up at MCA's theme parks next year.

Montgomery, son of Great Western Bank Chairman James F. Montgomery, says Dad didn't help him buy Harvey. He swung the deal with well-heeled friends he met getting his MBA at the University of Southern California and later as a Columbia Pictures film producer. Projected at \$5 million this year, Harvey Comics' revenues are up fivefold from 1989 and should generate \$1 million this year in pretax profits, a 30% hike from last year. Richie Rich would certainly approve.

By Ronald Grover in Los Angeles



WASSERSTEIN AND PERELLA INSIST THAT BUSINESS IS PICKING UP—AND SOME SAY BRUCE IS WORKING ON BETTERING HIS IMAGE

WASSERSTEIN PERELLA: THE RISE AND FALL—AND RISE?

Despite a long lull, the firm is expanding in trading and underwriting and pushing into Europe

In many ways, Wasserstein Perella & Co. seems the archetypal Wall Street story of rise, decline, and fall. Started in February, 1988, by Bruce Wasserstein and Joseph Perella, defectors from First Boston, "Wasserella" became one of the most successful investment banking boutiques of the past decade.

But in late 1989, the bad news began. The huge Federated Department Stores Inc. buyout that Bruce Wasserstein advised on began slipping toward bankruptcy. Then, last January, former client Interco Inc. threw an \$89.5 million malpractice suit at the firm for giving bad advice, which Wasserstein is fighting. And its role in the deal business has shrunk from third in 1989, according to Securities Data Co., to 10th in the first

half of 1991. "Wasserstein Perella was like a solar eclipse that is startling in its brilliance but passes away quickly," says one delighted competitor.

'BREATHING FIRE.' Wasserstein's rivals may be writing him off too soon. He's fighting back with the same aggressiveness that he made his name with. Rather than scale back his ambitions and cut costs, like his better-heeled competitors, he is forging ahead with a broad-based global expansion strategy. The firm just hired high-priced talent in Europe in a concerted effort to establish a stronger presence. Somewhat belatedly, it is diversifying into underwriting. "Bruce still comes into the office every day breathing fire," says a colleague.

As confident and ebullient as ever,

Wasserstein denies that past mistakes have hurt business and points to a recent flurry of activity not yet reflected in the deal standings. He says his company advised on 10 deals worth \$2 billion in the last two weeks. That includes two high-profile assignments reported on July 22: representing Cetus in its stock swap with Chiron, and Amev, the large Dutch insurer, in its bid for Mutual Benefit Life Insurance assets. "We had 70 deals that went wrong," Wasserstein says, referring to Federated and Interco. "But we had three deals that were the best deals ever—Beecham and SmithKline, Philip Morris and Kraft, and Georgia Pacific and Great Northern Paper Co. The fact of the matter is, were we doing O. K. to better than O. K."

the question remains whether Wasserstein Perella has overcome perhaps its most intractable problem: Wasserstein himself. Many press articles reported criticism of his deal tactics, shareholders, clients, and the courts. Wasserstein has been accused, for example, of putting his own interests ahead of his clients'. A spokesman says that "obviously, criticism never helps." But since the firm has a strong client base and all transactions are profitable, he adds, Wasserstein's reputation must be an asset. "The associates say he is working to change this negative image. 'Bruce has said he is mortal,'" says an executive at Nomura Securities, the large Japanese securities firm that bought a 20% stake in Wasserstein Perella in 1989 for \$100 million and is having its image problems these days. "His stress is under extreme pressure, and he is to change his arrogant attitude." When Wasserstein Perella began in 1988, the cockiness seemed justified. Its clients' goal was nothing short of getting into the ranks of Goldman Sachs and Morgan Stanley to be as good as Wasserstein Perella put it, the "hard Frères of the 1990s," and they nearly succeeded. The idea was to shun capital-intensive trading and be a classy, old-fashioned partnership that lived off its close personal relationships with the top of industry. Wasserstein Perella jumped into the leveraged deal business as well, with a \$1 billion fund.

SLIPPING MARKET. Profits were strong for the first 18 months. But in 1989, the deal business fell off a cliff. Most Wall Street firms backed their mergers and acquisitions departments and started focusing up their trading and underwriting departments. Not Wasserstein Perella. With the exception of its foray into junk-bond trading, it stubbornly remained an

firm focused on an ever-narrowing market—advising on big, hostile deals—that barely exists today. The numbers tell the story. Through July, 1991, Wasserstein Perella advised on only 10 deals, earned no disclosed fees, and had a 5.1% market share. That's down from 56 deals in 1990, which earned \$40.6 million in disclosed fees and garnered a 20% share. The firm squeaked in at 10th place for 1990's first half by working on \$8.4 billion worth of deals. But \$7.4 billion of that was due to its tenuous involvement in Matsushita's purchase of MCA Inc. Japanese staff at Wasserstein's venture with Nomura was a secondary advisor to Matsushita.

The jury is still out on how well Wasserstein Perella's LBO fund will perform.

Wasserstein has been cutting compensation—but he refuses to axe staff

In its haste to score the biggest LBO in Britain, it tied up a big chunk of its \$1 billion fund in Isosceles PLC, a supermarket chain that its management is trying to upgrade. While there is talk that the firm might sell its 40.2% stake next year, its \$340 million investment is more than double Isosceles' current market capitalization, says a Salomon Brothers analyst. KDI Corp., a conglomerate it bought with management in 1988 for \$260 million, had to be restructured this year. Wasserstein Perella ended up losing its \$10 million equity investment. Wasserstein says the fund's three other deals are going well. "We continue to do well as principal investors. We think we have made major, built-in profits."

The firm has been aggressively trying

to lean times have increased tensions within the firm, over which Wasserstein maintains tight control. He has been cutting compensation but has steadfastly resisted reducing his staff of 120 professionals and 120 support people. Indeed, he says he is even hiring. "There's a lot of ego at stake," says a competitor.

Wasserstein insists the good news far outweighs the bad. The firm's junk-bond business, started in mid-1989, has been lucrative. The 12-person trading desk makes money trading for clients and itself. Clients give it high marks. "It's pretty neat that you have a small firm in there that competes with much larger, better-capitalized competitors" such as Salomon Brothers and Merrill Lynch, says Dan Harmetz, a portfolio manager at Fidelity Investments.

The firm now hopes it can leverage this into expanded trading and underwriting. It hired Luis Mendez, a well-regarded trader from First Boston, to build its underwriting capability. And Wasserstein Perella recently got its first assignment: underwriting \$50 million of the \$2.7 billion Time Warner rights offering.

Time Warner isn't the only long-standing client that seems to have stayed loyal to Wasserstein Perella. Philip Morris, which hired Wasserstein for its 1988 takeover of Kraft, says it would hire him again if the situation merited it. "We maintain an ongoing relation with Bruce Wasserstein, as we do with other investment bankers," says Hans Storr, the chief financial officer of Philip Morris.

To revitalize his European operations, Wasserstein is recruiting local talent. The new team includes Lord Haslam, the ex-chairman of British Coal, British Steel, and former deputy chairman of ICI, and Sir Peter Levene, ex-head of procurement at Britain's Ministry of Defense. In Italy, Franco Reviglio, a former finance minister, just joined. And in Germany, Helge Petersen, who ran the Thurn & Taxis empire, one of the country's largest private family fortunes, is on board.

But the bad news may not be entirely over. An examiner's report in the Interco case will be released publicly in September, containing the first indication of how strong Interco's case is against Wasserstein. And most analysts agree that the firm will need a turnaround in the deal market or lots of staying power for its diversification strategy to bear fruit. But in the words of a competitor, "the one thing about Bruce is, you can never count him out."

By Leah Nathans Spiro in New York, with Blanca Riemer in Paris and Stephanie Cooke in London

SLOWER DAYS FOR WASSERELLA

	Number of deals*	Share of total market	Disclosed fees Millions
1988	25	24.8%	\$43.3
1989	52	50.4	82.1
1990	56	19.6	40.6
1991†	10	5.1	0.0

*COMPLETED M&A TRANSACTIONS WHERE WASSERSTEIN PERELLA PROVIDED ADVICE

**UNDISCLOSED FEES ON PRIVATE DEALS NOT INCLUDED

†THROUGH 7/17/91

DATA: SECURITIES DATA CO.

to break into investment banking in Europe, but with negligible success. Unlike its U.S. rivals, Wasserstein hasn't shown up on listings of big European M&A players. In April, 1990, it teamed up with Banque Paribas, Germany's Commerzbank, and Holland's Amro bank, to create the \$344 million European Mezzanine Fund. They bragged that it was the largest such fund in Europe. But to date, not one cent has been invested.

STILL HIRING. The European slowdown has lost the firm some talent. Last April, Jean-Luc Biamonti, who ran the firm's Paris office, quit to become vice-chairman of Crédit Lyonnais' investment subsidiary. In July, No. 2 Yves Alexandre quit to go to Goldman Sachs. Both say they resigned on good terms.

THE MARKET MAY BE ABOUT TO 'START ACTING UGLY'

After reading the charts, technical analysts see a thud coming

To the untutored observer, there is nothing terribly ominous about a chart of the Dow Jones industrial average. Up goes the line in January and February, when the Dow surged by 400 points, before making brave—if fruitless—forays at 3000. It hasn't gone much higher, but it's trying, no? Well, to professional chart-watchers—stock market technicians—the squiggles in the chart are fraught with danger.

From Gainesville, Ga., home of the widely followed *Elliott Wave Theorist* newsletter, to Wall Street, where Merrill Lynch & Co. technical analysts are espousing caution, technicians are widely predicting grim tidings for the market. They expect stocks to increase substantially during the summer, perhaps rising well above 3000 on the Dow, with a thudding decline thereafter. Indeed, some analysts are warning of a possible reprise of the events of 1987—when the market rose to record levels during the summer, only to crash in October. "Our work strongly suggests that the market is going to form a major top in the second half," says Dave Allman, director of research at *Elliott Wave*.

The technicians' skittishness flies in the face of generally upbeat convention-

al sentiment among institutional investors and brokerage analysts—and that's not too surprising. Unlike analysts, who examine market fundamentals such as earnings trends and future dividend flows, technicians examine statistics based on price and trading volume. The aim is to get a handle on the supply and demand for stocks, which determine the direction of prices.

When technicians aren't poring over statistics, they are eyeballing charts—and that's one area in which, some maintain, the market clearly displays weakness. The American Stock Exchange Composite Index, for example, is showing signs of a "double top"—often an indication that the market is about to reach a peak (chart). Likewise, the Dow's seesaw-like motion—its adherence to a narrow "trading range"—is also viewed by many technical analysts as a portent that the market is far from a picture of health.

OUT OF BREADTH. Many technicians are also expressing qualms about the market's lack of "breadth." Breadth indicators include various formulas that compare the number of stocks that advance to those that decline. The higher the breadth, the more stocks are participat-

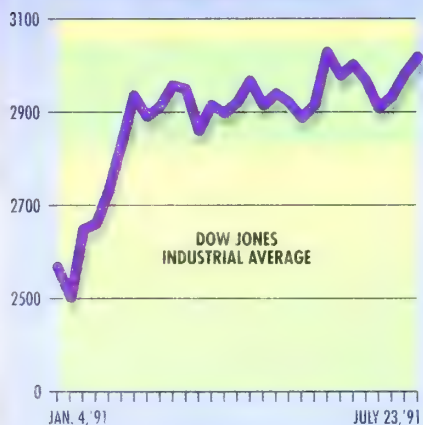
ing in the advance of the stock market indexes. And indeed, a decline in breadth was one of the earliest technical indicators of the market's weakness in 1987. Once again, some technicians maintain the market is riding for a fall. "This has been a very mixed market. The old story about this being a market of stocks, and not a stock market, has never been more true," says Stan Weinstein, editor of *Professional Tape Reader* newsletter.

To Weinstein, the most telling indicator of the market's weakness, despite its occasional rise above 3000, has been the failure of most stocks to join the Dow in rising to record levels. He notes that each time the market has broken above the 3000 number in recent months, it invariably failed to take very many stocks with it. When the Dow closed over 3000 on Apr. 17, 694 stocks joined the Dow in reaching new highs. But the next foray over 3000, in May, only half that number reached new highs. More recently, on July 18, the number of stocks celebrating new highs was just 220.

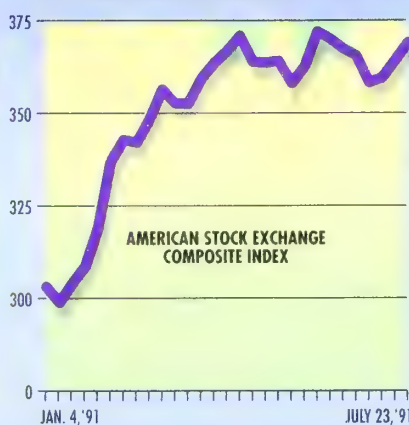
If well-known technical indicators such as breadth gauges are sobering, too are a host of lesser-known ones that are followed by market professionals.

WHY TECHNICIANS ARE GETTING NERVOUS

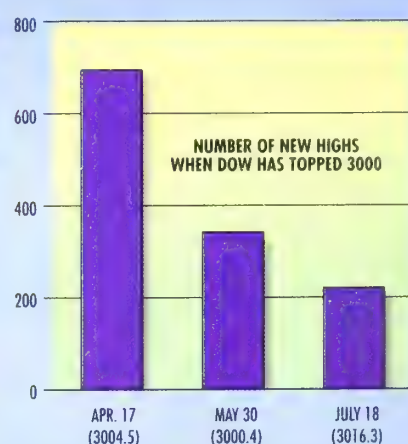
THE MARKET IS IN A NARROW 'TRADING RANGE'...



...WHILE THE AMEX IS IN A PERILOUS 'DOUBLE TOP'...



...AND FEWER STOCKS REACH NEW HIGHS



DATA: BRIDGE INFORMATION SYSTEMS INC., BW

trader and technician, Long Island's Richard Diamond, notes that the signs that are signaling caution in a "bellwether" index that combines IBM and General Motors share. He also uses formulas that work on volume data and analyse the number of new stock-price highs and lows. Diamond: "I don't really care about the formula, so long as it works."

'FULFILLING.' Long-term technical analysts are of crucial importance to investors and options traders, even if they hold positions for longer than a year so. Traders watch for a confluence of both long- and short-term trends,

as a way of predicting short-term market moves. Thus Diamond, who gives seminars on trend-based trading, is closely tracking long-term indicators even though he is a short-term trader. "The market has more to go before it reaches a top—maybe 3200 or 3300—but I don't know when that will be," says Diamond. "But at some point it is going to start breaking trend lines and acting ugly."

Technical analysts, however, did not predict the crash of 1987—even though some technicians, including Merrill Lynch's Robert Farrell, were sounding cautionary notes through the preceding

summer. Now, Merrill technicians are predicting a rise in the Dow to perhaps 3100 before a decline of 8% to 12%.

Richard McCabe, manager of Merrill's market analysis department, concedes that this is hardly a unique sentiment. And that may be the most ominous aspect of the technicians' wariness. "If this really is a popular notion and money managers become concerned about it," McCabe points out, "it might become a self-fulfilling prophecy." And when money managers start stampeding for the exit door, the rest of us can only follow—or be trampled.

By Gary Weiss in New York

FINANCIAL SERVICES

MAKE THE BEST PIES IN MINNESOTA'

Meet Harvey Golub, the nice guy now No. 2 at American Express

However powerful the post he has just assumed at American Express Co., Harvey Golub likes to make clear that he remains a gentle and modest fellow. *The New York Times*, announcing his appointment as president of AmEx and joint occupant, with Chairman and CEO James D. Robinson III, of the new "office of the chairman," mentions his love of baking and quoted Golub as boasting: "I make the best pies in Minnesota." Golub playfully asked that *WEEK* take special care in printing a photo, apologizing that "the material's not great."

Certain humility will serve Golub in taking the No. 2 spot at AmEx—just since Louis V. Gerstner Jr. shipped two years ago to run RJR Inc.—Golub will share the work with Robinson in running the company. President, he reports to Robinson, AmEx' five operating units and core staff will report jointly to the two. Still, because the two are contemporaries—Robinson is 55, Golub 52—and because Robinson intends to stick it out, Golub doesn't harbor ambitions of coming top dog.

TECHNICAL SKILLS. "My job is to help," he says. He is described by nearly everyone as highly intelligent, firm, well-liked, someone who "doesn't pull punches" and whose performance in running AmEx' IDS Financial Services—and his technical skills and detailed approach—expected to be a big boon in helping Robinson shore up some of the weaker parts of the company. Shearson Lehman Hutton Inc. is still pushing to effect a

turnaround, and AmEx' flagship travel-services business is smarting from the recession and heightened competition.

Golub has actually been working closely with Robinson for some time: He became vice-chairman last September and spent recent months shuttling between his home in Minneapolis, where IDS is based, and New York. Now, Golub will move his family and two Dobermans (who are "warm and friendly," he says) to New York. He remains chairman at IDS, but President Jeffrey E. Stiefel will now assume the title of CEO.

One insider says employees are "thrilled" with Golub's appointment. But even if Robinson should leave before expected, Golub would not necessarily succeed him. "Harvey is clearly No. 2, yet we have some very competent and talented people for the board to look at to fill any number of senior jobs," Robinson says. One person often mentioned as a potential successor is Howard L. Clark Jr., now CEO of Shearson and the son of AmEx' former chairman.

Golub says he will be quite happy to finish his career as president of AmEx, thank you, adding that he's held a number of jobs less

glamorous. The native New Yorker worked as a ditchdigger, waiter, and in the hardware department at Sears while putting himself through college. He graduated from New York University with a degree in business, and became a systems engineer at IBM after that. Golub also took three years out from a 14-year-career as a McKinsey & Co. consultant to serve as president of a Cherry Hill (N.J.) trucking company. He was fired, he says, because he disagreed with the owner over strategy. The company later filed for bankruptcy.

STAR EARNER. Golub's springboard to AmEx was his work at McKinsey, which included advising AmEx' Travel Related Services Co. He championed the quality-management program, which guarantees cardholders replacement cards within 24 hours, among other things.

When AmEx bought IDS in 1984, Golub left McKinsey to become its CEO. He added new businesses such as brokerage services, and made the unit a star earner for AmEx. When AmEx' second-quarter profits dropped 20% this year, partly because of \$171 million in write-offs at Shearson, IDS' net was up 19%.

Robinson says Golub's reputation has excited investors. The day after his new job was announced, AmEx' stock rose 1%, vs. a 30-point market drop. Analysts attribute the rise to better-than-expected earnings, but some people think Golub's appointment played a part. Says Robinson: "It was reflecting the fact that we now have a baker as president." If only the new president can make earnings come out as sweet as his pies.

By Andrea Rothman in New York



PRESIDENT GOLUB SAYS HE'S NOT CHASING JIM ROBINSON'S JOB

SOUTHEAST BANKING KEEPS HEADING SOUTH

The Florida ex-highflier is now bait for another bank—or the FDIC

In its ads, Miami-based Southeast Banking Corp. likes to portray itself as the place to go when trouble's brewing—that's when it's "time to call Southeast." Now it's Southeast that is looking for help. Once the dominant bank in one of the fastest-growing states, \$12 billion Southeast has been suffering a rapid deterioration, which could make it one of the next banks to

be taken over by the Federal Deposit Insurance Corp. or bailed out by a competitor. First Union Corp. is considered the front-runner, and Barnett Bank Inc. and BankAmerica Corp., are said to be interested.

The bank has posted six straight quarterly losses, including \$117 million in the first quarter of 1991. More losses are expected in the second quarter. Nonperforming assets at the quarter's end were \$776 million, 60% more than a year ago (chart).

COST TRIMMING. Douglas E. Ebert, a 22-year veteran of Manufacturers Hanover Trust Co. who took over as Southeast's chief executive officer in January, 1991, is busily working on damage control. Ebert and other Southeast officials would not comment. But his apparent strategy seems simple: trim costs, downsize, and seek an infusion of capital so the bank can go it alone. Southeast acknowledged on July 3 that it is having exploratory talks with regulators about the possibility of an "assisted transaction involving a merger or a significant amount of new equity." The FDIC will not comment.

Getting Southeast back on its feet will be no easy task. Its customer base is shrinking. "They've been losing a notable amount of deposits as people become worried about the bank," says Richard Stilling, a bank analyst at Keefe, Bruyette & Woods Inc.

Southeast's once highly profitable corporate banking franchise has been especially hurt. Several major clients have pulled their business. They include St. Petersburg-based Raymond James & Asso-

ciates Inc., the brokerage firm, and Miami's Wackenhut Corp., the security service firm. Wackenhut had banked at Southeast for 34 of its 36 years in business but began switching accounts to NCNB in December, 1990. Deteriorating service spurred the change, says Wackenhut Chief Financial Officer Michael A. DiGregorio: "They became a lot less flexible. We needed a banking environ-

ment that was going to support s-

Then there are Southeast's cat-woes. Last July, it promised the Controller of the Currency it would keep capital ratio requirements above minimum industry levels. So far, it has failed to maintain those levels. The bank until early August to submit a capital plan to the Federal Reserve Board. During a major upsurge in losses, however, analysts and regulators believe Southeast should avoid a liquidity crisis.

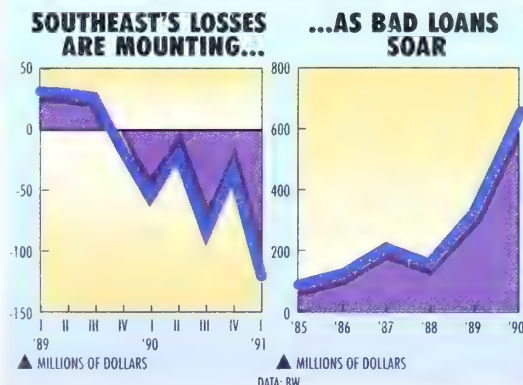
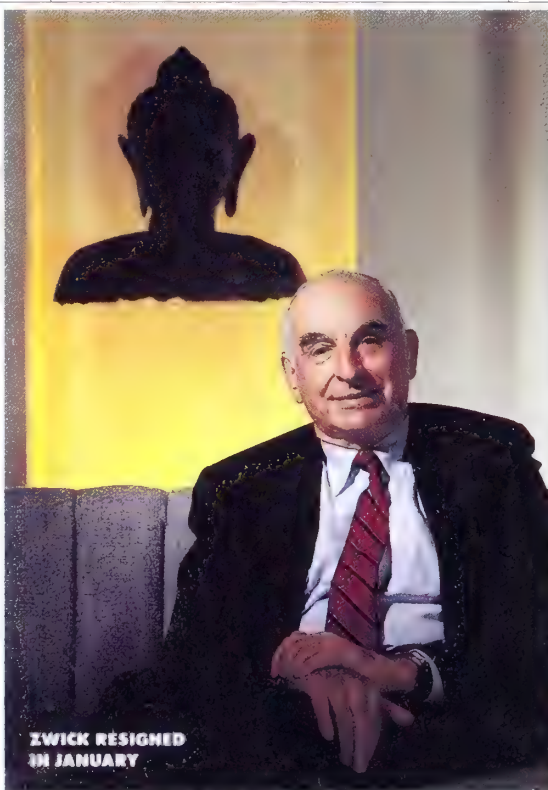
Such troubles would have seemed conceivable a decade ago, when Southeast towered over its rivals. At the helm was Charles J. Zwick, an autocrat and Harvard-trained economist who ran the Office of Management & Budget under LBJ. His biggest mistake was ignoring the growing retail market, preferring to focus on corporate clients. But Florida was never a bastion of corporate headquarters, and the 1980s mere wave thinned its customer base.

By the time Southeast reeled from its errors, rivals such as Barnett Banks, NCNB, and First Union had built up strong leads in consumer banking. "It boggles the mind that they missed the consumer retail market in Florida," says analyst J. Frederick Meinke at Raymond, James & Associates. As losses from soured loans piled up, Zwick came increasingly under fire. At a shareholder meeting in April, 1990, several investors urged him to resign. Finally, in January, under pressure from regulators, the board forced Zwick out. Zwick's lawyer says it isn't fair to blame Zwick for the bank's woes.

'CASE STUDY.' Most analysts believe that either through a merger or an FDIC takeover, Southeast will survive long for this world. One Southeast official with plenty at risk who is watching the situation is Alfonso Fanjul, a bank director. He headed the bank's executive committee and is its largest investor, with about 1.6 million shares, or 4.7%. Fanjul would not comment, but his attorney says his client has not written off Southeast. A government-sisted buyout might wipe out Fanjul and other shareholders.

Not that they haven't taken enough of a beating already. Since the end of 1988, Southeast's stock price has plummeted from \$22.50 to under \$2. "Southeast is going to be a case study of missed opportunities," says consultant Kenneth Thomas. "It was a big name that went nowhere." Except downhill.

By Antonio N. Fins and
DeGeorge in Miami



GENE G. MARCIAL

S. STEEL IS MORE THAN JUST A NOSTALGIA PLAY

Now that U.S. Steel is again trading as a steel company, after being split out of USX, a number of investors are coming back to cheer. No, it's not nostalgia that's drawing them—just old business fundamentals. Never mind that the Street is ignoring the stock, which started trading on the Big Board on May 7 at \$22 a share. Recent buying by some smart-money investors pulled it up to 25. These pros are betting that the stock will double within the next 12 months.

Optimistic thinking? Not at all, says investment manager Bob Gintel, who runs a mutual fund, with assets of nearly \$100 million. In recent years, he notes, U.S. Steel has drastically restructured, slashing fixed costs and streamlining its operations. USX shareholders approved on May 6 a recapitalization that divided USX into two—the USX-U.S. Steel Group and the USX-Marathon Group, the company's non-steel unit. The steel group includes diversified businesses, such as real estate, and financial activities. "It's the time," says Gintel, "to snap up Steel—when the shares are still unpopular and way undervalued." The Street, he says, has yet to recognize U.S. Steel's robust earnings power as the company picks up demand for steel. This year, Steel will be in the red, Gintel concedes, but that's the bottom. Next year will be in the black next year, figures Gintel, earning \$137 million, or \$2.70 a share.

The real impact of Steel's cost-cutting and efficiency efforts will come in 1993, Gintel expects the steel operations to produce earnings of \$865 million. For that year, he sees total company profits of \$530 million, or about \$10.50 a share.

Analyst Paul Kuklinski of Cowen & Co. is another bull who says that Steel is selling at a big discount to other steel companies. "With the recent write-offs of its last major unprofitable facility and the completion of its big capital spending next summer, U.S. Steel will be the most efficient, low-cost domestic integrated steel company, capable of competing in world markets," he says. U.S. Steel wants to sell assets from its non-steel businesses worth about \$1.5 billion. "If money could be used, he says, to pay off debt and buy back shares.

U.S. STEEL: PICKING UP NEW STEAM



DATA: BRIDGE INFORMATION SYSTEMS INC.

The stock, says Kuklinski, could hit 50 even before the end of the fourth quarter, when earnings are expected to start showing up. Based on 1993 estimates, he says, his ultimate target for the stock is \$64 to \$72 a share.

THE BLOOM IS ON THIS WALLFLOWER

For a little-known small pharmaceutical company that's yet to make any money, Belmac has been a surprise winner recently. Its shares have jumped on the American Stock Exchange from 5 in mid-June to 8½ on July 23—for no apparent reason. What's Belmac's secret?

"After 15 years of promises and delays, Belmac is finally making the transition from a development stage to a product-oriented and revenue-generating company," says Dennis Roth, an analyst at Chesapeake Securities Research in Towson, Md. He predicts that Belmac will be marketing two new-generation drugs shortly in Europe and in the U.S. by late 1992. One is called Biolid, a macrolide antibiotic for use against several common bacterial infections. The other drug is Alphanon, a transdermal treatment that Belmac says stops hemorrhoidal bleeding.

Roth estimates that Biolid and Alphanon will produce profits of \$1.86 a share in fiscal 1993, based on projected sales of \$64 million. Belmac has filed an application with the FDA to market Alphanon and Biolid in the U.S., and Roth expects approval in a year or so.

Mike Harshbarger, an analyst at HealthCare Capital Group in Chicago, estimates that Biolid alone, which was

granted a European patent last month and is expected to be marketed in France in autumn, will generate sales of some \$15 million in fiscal 1992, ending June 30. He expects Belmac still to be in the red in 1992 but sees Biolid's sales jumping to \$30 million in 1993. "Biolid alone will produce earnings of about \$1 a share," he says.

One New York money manager says Belmac's prospects have prompted several U.S. and European financial groups to offer it equity investments, as well as joint ventures. One French company, he believes, will soon buy a 10% stake. Belmac declined comment.

FIRST INTERSTATE: A BANK TO WATCH

Speculating on takeovers of troubled banks is a dangerous game. If you're wrong, you're stuck with a sick bank. But here's one low-priced bet that some pros say has a potentially high reward: the Class A shares of First Interstate Bancorp. There are some 43 million of them, trading on the Big Board at ⅞, or 56¢ a share. They shouldn't be confused with Interstate's common stock, now trading at 28. What the pros are buying are the Class A shares. In a takeover, they could fetch about 10 times the current price.

Here's how: The Class A shares were issued by Interstate in its 1988 acquisition of Houston's Allied Bancshares. According to the terms of that deal, if First Interstate is taken over, the acquirer would have to pay \$6 a share for the A stock. But to hit the jackpot, First Interstate would have to be taken over within 17 months. That's because the shares convert into common in January, 1993—using a conversion formula that, given the Texas subsidiary's poor results, would likely render them worthless.

Interstate has repeatedly insisted on independence. But if the recent mergers turn into a stampede, Interstate may have to give in. It doesn't have many friends, especially after posting a \$1.43-per-share second-quarter loss and slashing the quarterly dividend to 30¢ a share from 75¢.

BankAmerica, which is on the prowl for acquisitions, is an often-mentioned suitor. In a recent conference call with analysts, BankAmerica execs said they hoped that the Chemical-Manny Hanny match-up would change the mind-set of managements still resisting mergers. Some pros took that as a veiled message to Interstate's management.

By Jeffrey M. Laderman

BARNSTORMING



CLASH OF THE PUGIL STICKMEN: THE OBJECT HERE IS TO KNOCK THE OTHER GUY OFF HIS STAND

WHAT HAS FOUR LEGS, A COAT OF OIL, AND BOFFO RATINGS?

American Gladiators, the TV phenom, takes its show on the road

Zap is back! Zap is an original star of *American Gladiators*. She sat out last season's taping of the syndicated television show to have a baby. But this September, professional bodybuilder and onetime paralegal Raye Hollitt will be back on the job—pummeling volunteer masochists aching to act out their fantasies on national TV. What she'll find is a show whose appeal has broadened dramatically, and one that is fast spawning a cottage industry.

American Gladiators was conceived as a beat-'em-up arena attraction akin to professional wrestling. But unlike wrasslin', the outcome of the contests isn't predetermined. Contestants challenge each other in an elimination derby, with the eventual winner earning the right to take on the Gladiators. They try to knock the Gladiators off seven-foot platforms with pugil sticks, long poles padded like boxing gloves at each end. They scamper up sheer 30-foot vertical walls with a Gladiator in hot pursuit. They play a two-on-two game that resembles a hybrid of basketball and a back-alley mugging.

Gladiators, adapted for TV by Samuel Goldwyn Co., a Los Angeles production house, was one of three made-for-TV

junk sports that premiered in 1989. TV critics, enamored of Qintex Entertainment Inc.'s flashy *Rollergames*, gave Goldwyn's show little chance of survival.

But a funny thing happened on the way to renewal time. *Rollergames* died after a 13-week run, while *American Gladiators* found an audience. Two audiences, in fact: "We're still reaching the 18-to-34-year-old beer drinker it was designed for," says Richard H. Askin, president of Samuel Goldwyn Television, "but kids turned out to be a pretty avid core of supporters for the show." Youngsters love its simple, cartoon-like heroes and unfeigned competition. By the second season, TV stations in many markets were running it twice a weekend, adding a daytime slot to the original late-night airtime.

And kids mean cash to Corporate America. So Zap and the other Gladia-

Coke and 7-Eleven Stores are sponsoring the tour, and Mattel is readying a line of action toys for Christmas

tors, including Nitro, Gemini, La Blaze, Lace, and Ice, will return to TV stations for their third season in fall, just about the time an *American Gladiators* video game goes on sale along with Gladiator vitamins and snacks. That's all just by way of prologue to the yearend rollout of Gladiator dolls, action figures, from Mattel Inc. Licensing income from Gladiator merchandise, estimated at around \$15 million a year, flows mostly to Goldwyn.

Keeping that Gladiators name in front of the public has kept Goldwyn and his stable of athletes extremely busy. Since May, the Gladiators have taped 10 shows, signed seven licensing deals bringing their total to 21, and cut a half-dozen TV commercials for Mattel. The video-game publisher Game Tek says "This is getting to be a full-time job." Dan Claitor, the most popular Gladiator and a former linebacker at San Jose State University,

AMATEUR NIGHTS. By September, the hours will get even longer. *American Gladiators* is going on tour, sponsored by Coca-Cola Co. and Southland Corporation's 7-Eleven Stores. The traveling troupe, New York-based producer, David Fisher Productions, expects to land more than 100 bookings, with guarantees running from \$10,000 to \$50,000. On the road, Gladiators will battle amateurs chosen from local tryouts and also take on a few local celebrities, such as TV sportscasters. The expedition will culminate in national finals in Las Vegas next May.

In essence, *American Gladiators* is an Electronic Age variant of 19th-century tent shows that traveled from town to town inviting all comers to wrestle a bear or go 10 rounds against the show's strongman. The public hasn't lost its taste for such contests, as evidenced by *American Gladiators*' TV ratings. Within and week out, it's among the top 10 hour-long weekend syndicated shows, averaging 4.2% of U.S. TV households. Professional wrestling is still far ahead with a 10% audience share, but its heyday as the chic junk sport is over.

Gladiators, by contrast, is just carving into its own. Tryouts for the coming season drew more than 10,000 weekend athletes to four elimination tournaments around the country. As expected, plenty of policemen, pipefitters, and personal trainers turned out. But so did the occasional attorney and physician. The final 48 contenders include a San Diego minister and a couple of chiropractors. Nothing else, the lineup of challenger and the show's success—is proof positive that Walter Mitty is alive and well in Televisionland.

By Larry Armstrong in Los Angeles



"You're going to do
 at to the cellular phone
 is commercial? Run
 it with a golf cart? I
 hope you guys know
 at you're doing."
 That was Lee Trevino's
 ction when he was told
 kind of abuse that was
 ore for the Motorola
 ro T·A·C™ Digital Personal
 mmunicator during the
 oting of his first commer-
 for Motorola.
 Well, not only was the
 ro T·A·C able to with-
 d the pressure of a
 vvy golf cart, but its dura-
 y thoroughly impressed
 Trevino.
 "I saw the Micro T·A·C

dropped, bumped, thrown
 and muddied," said Trevino.
 "They did just about every-
 thing," he added, "but hit it
 off a tee with a three wood.
 Yet, after all that abuse, it
 performed like a champ. It's
 obvious that the Motorola
 cellular phone is put
 together to stay together."

"A lot of people
 call me a dur-
 able player,"
 concluded
 Trevino, "and
 if I continue

to hold up as well
 as my Motorola
 phone, I'll
 be on the
 tour for a very
 long time."



MOTOROLA

The way we put them together sets us apart.

IT'S A SHAKIER PERCH FOR TOSHIBA'S LAPTOPS

Communications breakdowns made it misjudge the U.S. market

For all the recent doom and gloom confronting personal computer companies, there's one niche that has seemed invulnerable. Shipments of battery-powered laptops jumped 35% last year and are projected to nearly double in 1991. So when the U.S. subsidiary of the world's No. 1 laptop maker lays off about 250 employees, as Toshiba America Information Systems Inc. did in the first quarter of this year, something must really be wrong.

Since then, Toshiba's woes have multiplied. In April, the top-ranked manager at its Computer Systems Div., which last year accounted for roughly 45% of the unit's \$940 million in revenues, abruptly resigned. The profit picture dimmed in May, when the company slashed prices by as much as 33% to catch up with an industry price war. In June, it fired its exclusive distributor, substituting Tech Data Corp., a wholesaler that it had fired a year earlier. But Toshiba America has a more serious problem: For nearly two years, it has trailed the competition in bringing new laptop technology to market.

No one is writing Toshiba off, of course. In 1990, it passed Zenith Data Systems Corp. to grab the No. 1 spot in the market for battery-powered laptops, with a 21% share of the \$3.2 billion business (table). And its research and development resources rank among the best in the world. Toshiba was the first supplier to sell color portables, and through a joint venture with IBM Corp., it plans to make color screens for battery-powered laptops. It's also a leader in use of longer-lasting nickel-hydrate batteries. And it's pushing ahead with wireless communications for laptops.

But for now, the company that popularized IBM-compatible laptops five years ago is stuck with an outdated product line. Instead of competing with a handful of companies for a tiny slice of the PC market, Toshiba is now vying with more than 130 laptop makers whose wares account for more than 15% of all PCs sold.

Toshiba's biggest weakness is in notebook computers, compact laptops that slip easily into briefcases. The newest models come with up to 60 megabytes of disk storage and use versions of Intel



NISHIDA: THE TOKYO MANAGER SPENDS HALF HIS TIME IN CALIFORNIA

Corp.'s speedy 80386 chip. But most of Toshiba's product line is still made up of heavy, bulky laptops or notebooks that use slower chips. Many of its products, in fact, still rely on AC power, not batteries. "Toshiba is held prisoner by a horribly out-of-date product line," says Aaron Goldberg, senior vice-president at researcher International Data Corp.

That's hurting sales. The company won't disclose results for its computer operation but says that overall sales at its U.S. subsidiary—which also makes copiers and fax machines—grew only last year, down from 30% annually in previous four years. Recently departed Toshiba America Information Systems executives say its computer sales for six months ended Mar. 31 were 70% of units—down more than 35% from previous six months and more than half below the year-earlier half. That, they say, led to a \$20 million to \$30 million loss for the period. Kiichi Hataya, president of the Toshiba subsidiary, says the company was profitable for the year ended Mar. 31.

In addition, the former executives estimate that as of Mar. 31, inventories of aging products stood at between \$50 million and \$100 million. To work off extra inventory, in July, Toshiba closed manufacturing at its Irvine (Calif.) plant for two weeks. Now, the executives say, Toshiba's internal projections put its loss for the six months ended Sept. 30 at as much as \$50 million. Hataya will not say that because of continuing price wars, profitability is likely to suffer in the short run.

WRONG CALL. The inventory buildup occurred because Toshiba didn't catch the shift to notebooks. Toshiba's American managers asked Tokyo to design a notebook PC with a hard-disk drive and Intel's 80286 chip back in 1989, but to be told that it couldn't be done. So Toshiba's Tokyo-based designers were badly unprepared when Compaq Computer Corp. announced its LTE 286 that October. Toshiba's 80286-based notebooks arrived in February, 1990, but they were substantially larger and slightly heavier than Compaq's. Toshiba didn't release a slimmed-down version until last month.

Toshiba also missed with 800-based notebooks. It announced the line last November, along with other suppliers. But Toshiba's use of a slower version of the Intel chip because executives in Tokyo calculated that fewer 80386s would be in short supply. It was a business decision, not a technology decision, and we probably erred, says Dennis E. Eversole, senior vice-president of the American subsidiary. By the time Toshiba started shipping

STILL AHEAD IN LAPTOPS

Share of U.S. unit sales

TOSHIBA	21%
ZENITH	10
COMPAQ	10
NEC	9
TANDY	8
SHARP	8

DATA: INFOCORP

THE ONLY YARDSTICK THAT COUNTS.

Much has been written about various ways to measure corporate performance. But over the years, the odds on favorite would have to be earnings.

We think that a focus on earnings misses a much more relevant factor.

Free cash flow.

And once again, we expect ours to remain strong. Extremely strong. In fact, in a year when business has certainly not been booming, our free cash flow will run close to \$1 billion. And we expect that number to average substantially more in the coming years.

And the point?

Cash, not earnings, has put us on the fast track to debt reduction.

In fact, between cash from operations and the sales of certain non-strategic assets, we're well ahead of schedule. Which means we're adding economic value to the company more quickly than many thought we could.

To be sure, there are as many opinions on the subject of how best to judge value as there are people to pen them.

But we think we'll stick with cash. It sure works for us.

And we think it works for our shareholders.

Georgia-Pacific



underpowered T2000SX last February, other companies—notably Compaq, AST, and Dell—were already delivering the speedier machines. Worse, AST Research Inc. and Dell Computer Corp. were charging up to \$2,000 less than Toshiba. In July, Toshiba added the T2000SXe, a notebook that uses a faster version of the 80386.

SHORT LEASH. One reason Toshiba fell behind, say other computer industry executives, is the U.S. unit's strained relations with the parent company. Defections by key American executives in late 1988 and early 1989 led to "a breakdown in the working relationship and communications between the U.S. and Japan," says John E. Rehfeld, one of the computer division's first employees. He eventually became general manager but left in January, 1989, to become president of Seiko Instruments Inc.

Over the years, Rehfeld had built up

By the time Toshiba brought out its 386-based notebook, rivals were delivering faster models—for up to \$2,000 less

considerable influence with his bosses in Tokyo. But after he left, the Americans had less say. Unlike rival NEC Corp., which has transferred most design-and-manufacturing authority to its American subsidiary (box), Toshiba continues to design its laptops in Tokyo. And with product development in Japan, Toshiba has sometimes misjudged the U.S. market. For example, it pooh-pooed the need for high-capacity hard disks, which many American consumers require in laptops. "When things sour, all control is

pulled back to Tokyo," says David Carnevale, senior vice-president at market researcher InfoCorp. "It's the Achilles' heel of almost all U.S. subsidiaries of Japanese companies."

Toshiba executives say their American subsidiary is already on the mend. "We concede that they underinvested in engineering and are now spending more," says Atsushi Nishida, the Tokyo-based senior manager of Toshiba's computer market outside of Japan. That, he says, will result in "outstanding new products." This year, Nishida is allocating his own time to shore up the beleaguered U.S. operations. With the two top Americans at the U.S. division gone, Nishida is spending half his time in Irvine. For that kind of commute, he may need two laptops.

By Larry Armstrong in Irvine, Calif.
with Neil Gross in Tokyo

NEC IN THE U.S.: A DETOUR ON THE ROAD TO THE BIG TIME

When the laptop computer took off in the U.S., Toshiba America Information Systems Inc. took off with it. By 1988, it was giving Japanese rival NEC Corp. a run for its money. But NEC could still claim to be the biggest success among Japanese computer makers in the U.S. After all, it was doing well both in laptops and in desktops.

To do even better, NEC 18 months ago merged its U.S. laptop and desktop units into NEC Technologies (NECT) Inc. With the combined company's broad line and a retail network nonpareil among IBM-clone makers, NECT appeared set to be the first Japanese to really challenge the PC market leaders.

But NEC has been having some trouble. Combining the two units has taken longer than expected, partly because the company's withdrawal from the U.S. television and VCR businesses distracted managers. And the expected benefits from combining laptop and desktop marketing haven't materialized. Recent mergers of computer retailers have concentrated NECT sales into just two major chains. Result: NECT expects revenues for the year ending Mar. 30, 1992, to be flat with last year's \$992 million.

And that's the good news. Like Toshiba, NEC is finding U.S. competition far tougher in the hot market for notebook-size laptops. NEC's UltraLite, introduced in 1988, was the first notebook on the market. Now, NEC lags

rivals such as Compaq Computer Corp. and AST Research Inc. in both pricing and technology. NEC's notebook based on Intel's 80386SX chip, for instance, arrived eight months after others were announced. And it took NEC three months to match Compaq's spring price cuts on laptops.

DESIGNED IN THE U.S.A. Such delays have been costly. NEC's 9% share of the U.S. laptop and notebook market puts it in fourth place, far behind Toshiba, says market researcher InfoCorp. In desktop computers, the company's market share is now expected to de-

clined this summer, designed to be sold in computer superstores. Then, in September, a line of machines to connect networks of PCs. Aimed at corporations, they will be sold partly through a beefed-up direct-sales force. "This is what we've been working on the whole year," says James R. Berrett, NEC's chief operating executive.

The products are a big test for NEC. When the two units merged, American managers pushed for permission to design and build products specifically for the U.S. market rather than sell Japanese designs. Headquarters agreed, and the U.S. unit now develops and manufactures NEC's PCs for the Americas, Europe, and Australia.

To pull ahead in the U.S. and other markets, NEC has to make not only IBM's and Compaq's technology but also their new pricing. And—hardest of all—it must match their marketing skills. But NEC is making some progress.

KinderCare Learning Centers Inc. just bought 1,250 NEC desktops. Low prices helped, but NEC's willingness to customize the PCs clinched the deal, says John McKay, a KinderCare vice-president. NECT needs more such sales. It can't afford to lose another 18 months in its efforts to crack the PC big time.

By Gary McWilliams in Boston



**NEC'S
ULTRALITE
LAPTOP FELL
BEHIND IN
PRICING AND
TECHNOLOGY**

cline for the third year in a row, falling to 1.4% in 1991 from 1.9% in 1990, and 2.3% in 1989, says another researcher, WorkGroup Technologies Inc.

NEC Technologies is plotting its comeback—with new products and distribution plans. First up: a line of low-cost

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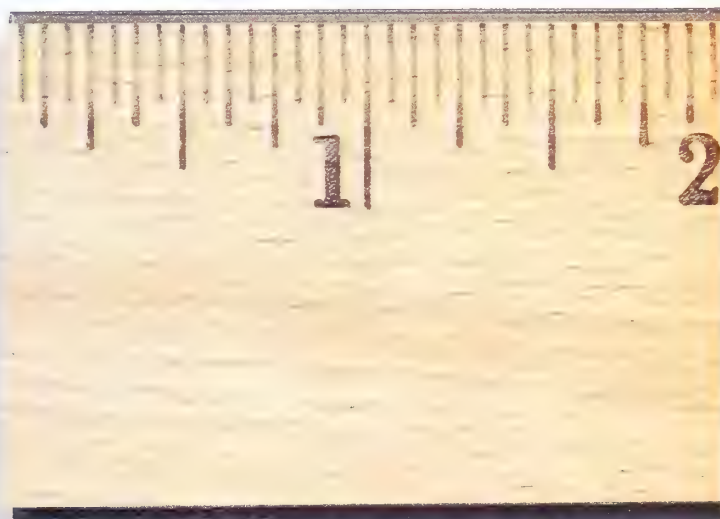
MOST AIRLINES THAT FLY TO SEA

Any airline can transport you from one place to another. Unfortunately, that's about as far as most airlines go. At Alaska Airlines, however, we like to take a slightly different approach. Like serving you good food, giving you a little extra legroom. In short, doing everything we can to make your trip as enjoyable as possible.



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RESEARCH

PUMPING UP THE BABY BELLS' R&D ARM

Fresh from TI, George Heilmeier is whipping Bellcore into shape

No one knows better than George H. Heilmeier that an earthquake is shaking Bellcore, the R&D arm of the seven phone holding companies known as the Baby Bells. When Bellcore's board lured Heilmeier from the top technology job at Texas Instruments Inc., it asked for "a culture change." Confronted with the computerization of phone networks and beset by new rivals, the owners of the nation's largest R&D consortium wanted faster product development and more progress in information technologies. After 13 years running a crackerjack R&D effort, Heilmeier seemed equipped to deliver.

Five months later, Bellcore's new president is doing just that. In nearly 170 hours of meetings with employees, Heilmeier has delivered a clear message: no more business as usual. The Baby Bells must "change to accommodate fast-moving technologies and a competitive environment," he says. "Bellcore will do the same."

LESS ACADEMIC. Heilmeier already has merged two budget operations into one. He promises to step up research in such information technologies as object-oriented computing, data bases, and multimedia, even if it means less work in the physical sciences, a tradition at Bellcore. Enhancing quality in product development and speeding up decision-making are also priorities (table). And there's one more: He wants Bellcore, with its \$1.1 billion budget, to set the agenda for future phone system technology.

The practical effect of Heilmeier's plan will be to junk the more academic approach to R&D set up in 1984, when Bellcore was created during the breakup of Ameri-

can Telephone & Telegraph Co. The Bell companies didn't want an R&D branch that dictated products and technology to them, as Bell Labs had done. So Bellcore was initially weighted down with 144 councils, committees, panels, and customer groups—and every decision had to be unanimous. Rather than recommend actions, the staff mediated different

proposals for technology and products. The lab churned out a raft of innovations—everything from lasers and batteries to sensors and chip manufacturing techniques. But too often, "it was search for research's sake," says Starliper, a project manager for Baby Bell. Or, oodles of features might be added to a product to satisfy all the Baby Bell owners. Projects became mirages, and costs and timetables took a backseat. For instance, maintenance software called OSS, for operations support system, was supposed to take years to develop. When it arrived this summer, it will have taken three. And will contain some 6,000 features.

The 55-year-old Heilmeier, who earned a PhD in materials and electronics at Princeton University, is well equipped to tackle such problems. As a young

engineer at RCA Corp., he made discoveries that led to the first liquid-crystal display. During the 1970s, as assistant director of research and engineering in the Defense Dept., he redirected and cut 270 projects totaling \$100 million, raising R&D efficiency. As director of the Defense Advanced Research Projects Agency (DARPA), he was instrumental in steering R&D on stealth aircraft, infrared technology, and space-based lasers. Former colleagues credit him with making TI's R&D world-class. He instituted what is known as "Heilmeier's catechism," a set of questions by which all projects are measured. The goal was to focus projects on TI's markets and objectives.

NO EXCUSES. Heilmeier is known for managing by a verbal contract—and holding people accountable. "George has little patience for excuses," recalls one TI researcher. Projects are canceled when promises aren't kept. An effort to produce a liquid-crystal display out of plastic instead of glass was such a victim at TI: Heilmeier deep-sixed the effort when its progress didn't meet the timetables set by its leaders.

Still, "it's George's ability to inspire people and influence what they do that sets him apart," says Floyd Hollister, vice-president of corporate staff at TI. He keeps "current across a wide



HEILMEIER'S GAME PLAN FOR BELLCORE

SPEED UP DECISION-MAKING

Researchers and managers used to spend a lot of time in R&D meetings. Now they're expected to be decisive.

SET STRATEGIC DIRECTION

With his board, Heilmeier has set a clear priority program for Bellcore.

IMPROVE QUALITY

Is emphasizing total quality management, including training for quality circles.

PAKE BUREAUCRACY

Is downsizing the controller's group 20% through attrition, other cuts to follow.

WORK INFORMATION SCIENCES RESEARCH

Is increasing work in object-oriented computing, data bases, and multimedia.

rum of technologies"—unusual for high-level technology executive, says Stover. That breadth of knowledge, some, is behind Heilmeier's knack for making the right calls on technology. These abilities will come in handy as Heilmeier tries to transform Bellcore into a technology leader. He took a first step in June, when he got Bellcore's mandate to identify seven priority projects. It also agreed to streamline decision-making by no longer insisting on unanimous decisions. And now, Bellcore's staff will recommend actions, not follow directives. That "will cut decision-making time," says Heilmeier.

Over the next three years, for instance, the Bell companies have been unable to choose among competing approaches to an Advanced Intelligent Network, which would let them offer new services without having to replace central phone switches. In July, Bellcore proposed a design direction that was accepted almost without change.

Heilmeier is also pushing to improve coordination and to develop closer ties with the company marketers. Changes are already rippling through Bellcore's software and systems group. At Heilmeier's insistence, the group is moving faster and planning to integrate object-oriented programming, which helps produce better software faster. "His experience with the technology brought us insight into its payoff that we hadn't had," says Robert L. Martin, vice-president of the group. Martin's group is also testing new services more extensively before shipping them to customers.

A HIGHWAY. But the biggest challenge lies in making Bellcore the leader in creating a national communications infrastructure. Over the next decade or so, the telecommunications industry will construct a network for data, voice, video, and text designed to carry information services into homes and businesses. Japan and Europe already have government-driven plans for such networks. In the U.S., the Commerce Dept. is leading the effort. But Heilmeier believes that no group is better suited to coordinate the project than Bellcore.

The lack of coordination so far has made the Baby Bells plenty. A new report from Bellcore by McGraw-Hill Inc.'s North-Business Information research firm says that logjams over standards have prevented any significant new national communications services from emerging since the breakup of AT&T. It won't until this year, for instance, after years of debate, that all the players, including the phone companies and makers of computer equipment, agreed on technical standards for the Integrated Services Digital Network, which is used to carry voice, data, and video over a single phone line. So far, Heilmeier is getting high

marks. "He's bringing fresh perspectives," says Joel Engel, an assistant vice-president at Ameritech Services, a unit of Ameritech Corp. Still, Heilmeier must perform a balancing act. The Bells want Bellcore to be a more effective leader. Yet they also intend to develop their own products. Says Matthew J.

Stover, Nynex Corp.'s top spokesman: "Bellcore is always going to be the least common denominator, and in technology, that's a dangerous place to be." Heilmeier's challenge is to push ahead without setting off too many tremors.

By Emily T. Smith and Peter Coy in Livingston, N.J.

THE MAN WHO'S RUNNING A NUTSIER-BOLTSIER BELL LABS

The forces reshaping Bellcore have not spared the granddaddy of communications research, AT&T Bell Laboratories, which is also under new leadership. "Bell Labs as an entity no longer exists," complains Charles V. Shank, an electronics expert recruited from Bell Labs last year to head Lawrence Berkeley Laboratories. Yet Shank becomes a pushover when asked about Bell Labs' new president: "John Mayo is an absolutely terrific choice."

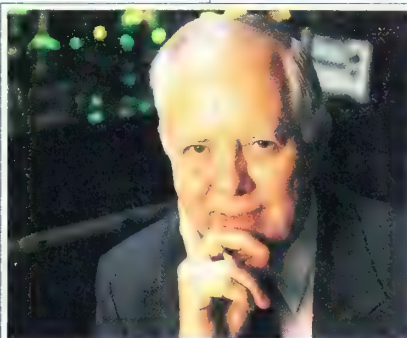
That's just the kind of endorsement John S. Mayo needs as he takes over from Ian M. Ross as the seventh president of the world-famous labs. Mayo will have to draw on a reservoir of trust and respect for his scientific acumen as he makes exactly the kinds of changes that worry scientists such as Shank. Mayo, named on July 1, plans to continue making Bell Labs more of a profit-minded industrial lab—and perhaps less of a breeding ground for Nobel prizes, of which it has produced four.

At 61, Mayo has four years to make his mark. He has already spent 36 years with Bell Labs, playing big roles in the first Telstar communications satellite and the first system for high-speed digital transmission of phone calls. He went on to be the executive in charge of switches and transmission gear—a job that gave him experience in meeting budgets and dealing with business types.

That should come in handy now. Bell Labs is the only arm of American Telephone & Telegraph Co. scarcely scathed by cuts. Its budget, slightly more than \$3 billion a year, has risen nearly 60% since the Bell System breakup in 1984, partly through taking over functions of other AT&T units.

Now, pressure is growing to produce

more tangible results. The 90% of the labs' budget that goes to development has been placed firmly under the control of the managers of AT&T's 20 lines of business. Even the \$300 million research section was reorganized last year to focus more on practical fields, such as information science, and less on the prize-winning physical sciences.



MAYO: BELL LABS' R&D CAN SATISFY BOTH SCIENCE AND THE MARKETPLACE

Getting approval for long-term projects is tougher than ever, says Al Cho, director of semiconductor research. Cho spent a dozen years co-developing the molecular beam epitaxy machine, a device for growing crystals that has become a mainstay of semiconductor research. He won-

ders if he could get approval for such a project today.

Mayo insists that there's no conflict between responding to immediate business needs and doing important research. He notes that Bell Labs' search for a replacement for vacuum tubes, which blew out too often, led to the transistor, one of the biggest physics breakthroughs of the century.

NO DAWDLING. As AT&T shows a new boldness—typified by its recent purchase of computer maker NCR Corp.—Bell Labs will have to be nimbler. Mayo says he'll remove speed bumps, such as lack of teamwork, that inhibit quick product introductions and new software. That stress on streamlining won't be easy to stomach for scientists who prefer the long view.

Luckily for Mayo, he goes in with plenty of goodwill on his side. Cho, despite his misgivings about the Labs' direction, says: "He's going to be an outstanding president." If Mayo can retain that kind of support, he should be able to make a real difference in his few years at the helm.

By Peter Coy in New York

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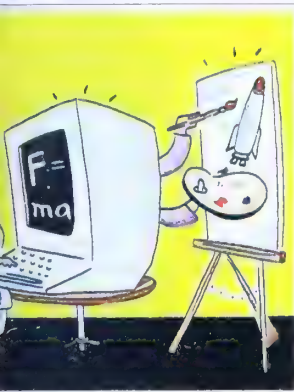
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Developments to Watch

BY EMILY T. SMITH

SOMETIMES, A PICTURE IS WORTH THOUSAND MEGABYTES



Researchers trying to simulate phenomena such as car crashes and hurricanes are having difficulty coping with all the reams of data produced by their supercomputers.

To help, IBM has just rolled out a specialized computer that can turn masses of numbers into highly detailed, full-color motion pictures. IBM's Power Visualization sys-

es as many as 32 reduced instruction-set computing processors, which together can execute 2.5 billion math operations per second. Adding to the machine's power is its ability to pull in, from another supercomputer, as many as 100 characters of information per second—more than most desktop computers can handle.

In promoting the machine, to be delivered later this year, IBM says that the troubled computer maker is learning how to get its products to market faster. The system, which costs \$1 million to \$2 million, was developed in about two years by a newly independent IBM team. Team members frequently consulted the design with potential customers but rarely called on the manufacturing and marketing departments.

SUPERCONDUCTORS WON'T GO TO PIECES

Since high-temperature superconductors were discovered five years ago, researchers have tried to make the ceramics stronger. But so far, most of the materials they have invented aren't robust enough for commercial use.

On July 22, at an international conference on superconductivity in Japan, researchers from Northwestern University and the Argonne National Laboratory announced the discovery of a new family of high-temperature superconductors that are stronger and more stable than earlier materials. They think these compounds will be much easier to form into wire or cable that can conduct electricity with no resistance.

The key to these new materials is substituting gallium for indium in the conducting material. In this new material, layers of gallium and oxygen atoms are sandwiched between layers of copper and oxygen atoms. It's the planes of copper and oxygen atoms that conduct electricity without resistance; in other materials, the copper-oxide planes are broken up by nonconducting elements. The researchers think this new material is what makes the materials, which become superconducting at -328F, less brittle than other superconductors.

BLOOD ANALYSIS IN HALF THE TIME AT ALL

Speeding up test results for intensive-care patients could save lives. Yet, when it comes to analyzing gases in the blood, doctors are forced to wait 20 minutes or more.

Now, PPG Industries Inc. is offering quicker answers. Its

biomedical division's StatPal Blood Gas Analysis System pinpoints, in about two minutes, the pH, oxygen, and carbon dioxide levels of the blood. Armed with these data, doctors can more quickly make decisions to enhance their treatment of heart attacks, pneumonia, and other life-threatening illnesses.

The device simplifies a cumbersome procedure. Currently, a technician draws a blood sample, submerges it in a bucket of ice to "freeze" the blood's metabolic activity, then carries the specimen to a lab. But at less than four pounds, StatPal can travel to the patient. Its sensors are housed in a disposable syringe. Once the blood is drawn into the syringe, the sensors "read" the gas levels in seconds. Results are simultaneously displayed on a small screen and printed out. Best of all, at \$3,000, the unit is one-tenth the cost of the older technology.

FLYING ROBOTS—WITH 'MINDS' OF THEIR OWN

On July 29, some rather strange flying machines will take to the skies over Atlanta's Georgia Institute of Technology in the first aerial robotics competition. The entrants, sponsored by universities and industry, will have one task: move half a dozen metal disks from one side of a volleyball court to another in three minutes or less. This seemingly simple chore is a true challenge for this new class of aerial robots. Unlike earlier flying robots that were radio-controlled by humans, these steel birds must locate, retrieve, and transport the disks without any human direction at all.

Although such robots are still experimental, advances in mechanical vision systems, computing power, and software have made them feasible. The machines, made from off-the-shelf technology, "show that autonomy in aerial vehicles is not that far off," declares Robert C. Michelson, vice-president of the Association for Unmanned Vehicle Systems. Flying robots could help cut costs or avoid risk to humans in a variety of ways. The military sees a use for them on battlefields to avoid exposing soldiers to hostile fire. They could also come in handy for monitoring utility lines or checking forests for disease.

WILL THE SILENT CHAIN SAW BE NEXT?

By this time next year, two noisy appliances—probably a range exhaust hood and a dishwasher—will turn silent. Sweden's Electro-lux has signed a \$2 million deal with Noise Cancellation Technologies Inc. (NCT) in Stamford, Conn., to use NCT's electronic antinoise technology in products.

NCT's technology detects sounds coming from the appliances and generates mirror-image sound waves that physically cancel out the offensive waves. Other Electro-lux items, such as rackety vacuum cleaners (sold in the U.S. under the Eureka label) and window air conditioners, would also seem ripe for the treatment, since NCT says its technology can help cut electrical consumption by as much as 50% in the two appliances. That's because many fans and motors are designed to minimize noise, at the expense of efficiency. With NCT's technology, this trade-off isn't needed.



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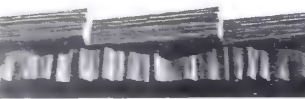
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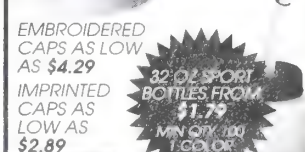
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BANKRUPTCY



SECOND-GENERATION STEELWORKER RABONE THOUGHT HIS FUTURE WAS SECURE

ARE INVESTORS LIABLE FOR LBOs GONE BUST?

In a landmark suit, Kaiser retirees raise this troubling question

Tom Rabone first laid eyes on Kaiser Steel Corp.'s huge mill back in 1946 after his dad found work there. By 1950, he was making steel at the Fontana (Calif.) plant, too. The work was often brutal, but pay and benefits were good: By the time Rabone retired in 1983, he and his wife had raised four kids, sending one to Stanford University. They looked forward to a generous pension and full medical coverage as long as they lived. "People felt there was some security that was assured," he recalls.

Then came Irwin L. Jacobs. Pressed by the Minneapolis raider, Kaiser went private in a 1984 leveraged buyout. Jacobs pocketed more than \$60 million for selling his stake in Kaiser, including \$14 million in greenmail. But under the new owners and the heavy LBO debt, Kaiser ran aground, unable even to pay health insurance premiums. By 1987, it had filed for

bankruptcy, leaving Rabone and more than 7,000 other retirees with slashed pensions and no medical insurance. "People were asking: 'Do I pay my bills and buy groceries, or do I buy my prescriptions?'" says Rabone.

Now, Rabone is hoping that a group of Kaiser retirees will be able to recapture some of the \$160 million in cash that the LBO paid to stockholders. Kaiser, on behalf of retirees and other creditors, is suing Jacobs and a slew of Wall Street firms, including Goldman Sachs,

Bear Stearns, and Smith Barney. A sue: Can public investors, and even brokers, be held liable for money made on an LBO if it later goes south? The defendants, of course, say no.

The case, awaiting arguments set Sept. 19 before a U.S. Circuit Court of Appeals, promises to plant a signpost in an expanding area of the law known as "fraudulent conveyance." This legal concept isn't new: The first fraudulent conveyance statute dates back to Elizabethan England. The term has less to do with fraud in the usual sense than it does with the transfer of assets out of an insolvent company—or an asset transfer that leaves a company with not enough capital to operate.

STICKY WICKET. Now, creditors are aggressively exploring ways to exploit fraudulent conveyance to failed LBOs (see p. 10). With the likes of Revco DS Inc. and Campeau Corp. in bankruptcy, fraudulent conveyance "is a hot topic right now," says Marty Harper, a lawyer for Kaiser creditors.

The legal principle behind this wave of fraudulent-conveyance cases is familiar, notes University of Chicago law professor Douglas G. Baird: If a business was insolvent at the time of sale, then its creditors—not those who sold the business—are entitled to its proceeds. "If I'm a debtor and you're a creditor," Baird explains, "one of the things I can't do is transfer my assets to escape paying you back."

Particulars of the current cases differ. But in each, creditors of the bankrupt company are trying to get back from selling shareholders—and, in some cases, lenders, accountants, and financial intermediaries—proceeds and fees from a buyout that sometimes was completed years ago. The Kaiser suit looms especially large because, among the pending fraudulent-conveyance cases, it's at the highest judicial level—just below the U.S. Supreme Court. "It will certainly color arguments in other cases," says Barry L. Zaretsky, a Brooklyn lawyer.

School professor is the court's examiner in the Revco case.

In trying to recoup money from stockholders and their brokers, the Kaiser plaintiffs have their work cut out. The lower court agreed with defendants that Congress in 1982 protected them from such suits. To maintain liquidity in the securities markets, the law shields payments made in

BIG FRAUDULENT-CONVEYANCE CASES

KAISER STEEL

Kaiser no longer makes steel, but for retired steelworkers and other creditors it's still seeking over \$200 million from investors and advisers who worked on the 1984 buyout

MCCALL PATTERN

Creditors are suing investor Reginald Lewis and lender Bankers Trust over the 1987 buyout. In a key July ruling, the court said financiers could be forced at trial to forfeit their fees

RESORTS INTERNATIONAL

Donald Trump paid \$16 million to settle fraudulent-conveyance claims by Resorts bondholders after his 1988 sale of Resorts International to Merv Griffin

REVCO

The drug store chain, now in bankruptcy, has dropped its fraudulent-conveyance suit against small shareholders and advisers involved in its 1986 buyout. It's still pursuing big investors and lenders

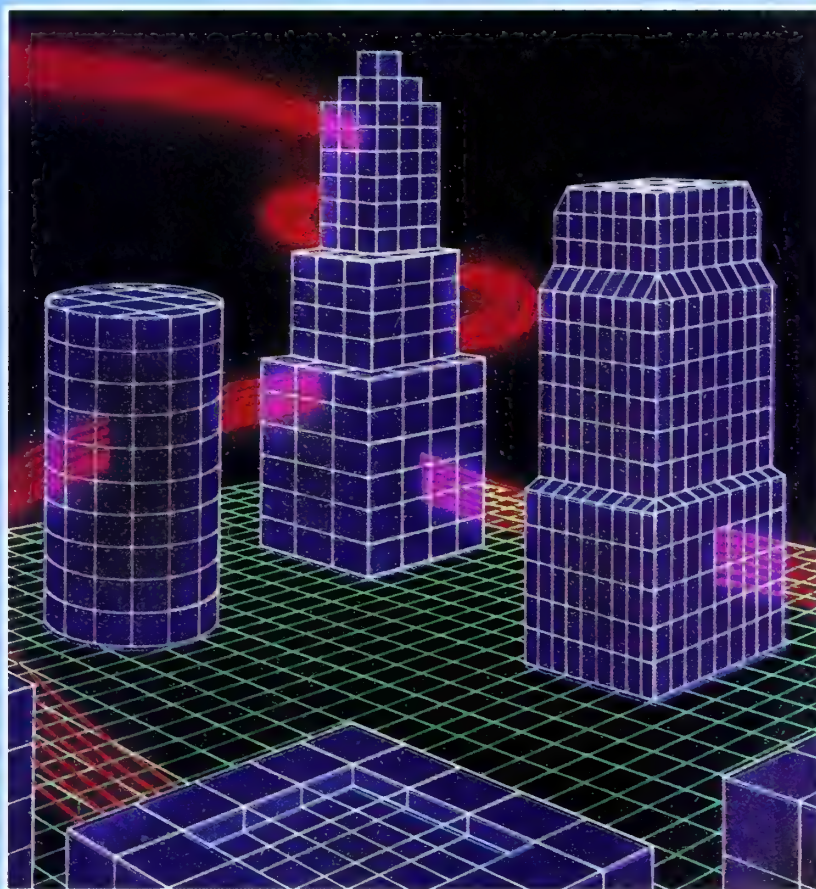
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chain of transactions that compose the clearing and settlement process—where, say, cash goes from a buyer to his broker, from the broker to a clearinghouse, from the clearinghouse to the seller's broker, and then to the seller. Last year, the appeals court upheld dismissal of the suit against mere "conduits," such as clearinghouses, but agreed to decide if brokers and investors may be sued.

FINE POINT. At the heart of Kaiser's appeal is its contention that the swap of stock for cash in an LBO is not a securities trade at all. Instead, Kaiser maintains that when it went private and investors turned in their stock, that deal was a "mandatory redemption"—and not, Harper says, something Congress meant to protect. Stockholders, he argues, shouldn't be able to use the settlement process to hide from creditors.

It's an excruciatingly technical point, to be sure. But it's also one that, given the last decade's craze for going private, could have a sweeping impact if the appeals court agrees. Consider: If investors could be held liable when they buy stock in a pending takeover that years later is deemed to be a fraudulent conveyance, they'll surely think twice, damaging liquidity. Citing the potential instability such a ruling could bring to the securities-settlement system, the Securities & Exchange Commission has filed court papers siding with the defense.

Even if the appeals court rules against Kaiser, Jacobs and his investment partners won't be finished with the whole affair. The lower court specifically excluded the Jacobs group from its dismissal of the suit against the others. Plaintiffs allege that Jacobs knew that Kaiser's huge unfunded liabilities, especially those for the retirees' medical benefits, made it insolvent before the buyout but that he went ahead and helped to strip the company anyway.

At that, Jacobs scoffs. Kaiser, he says, "was definitely a going concern." Kaiser's accountants, Touche Ross, came to the same conclusion, notes Jacobs' lawyer, Jerome B. Simon, who says that to challenge the audit "is Alice in Wonderland." Jacobs adds that Kaiser "just sued everybody they could find."

Rabone blames just about everybody, too, including Kaiser's former management and board, which Kaiser also sued. Kaiser in June settled that case for \$17 million. And, through a court-ordered trust, the Rabones now have health insurance. But coverage is less generous, and it costs them \$235 a month. Folks in Fontana are "hopeful we may be able to increase those benefits" through the suits, Rabone says. Yet the bitterness over the failed Kaiser LBO remains.

By Robert Barker in Fontana, Calif., with David Greising in Chicago

Marketing

TOYS

'HAS-BEENS' HAVE BEEN VERY GOOD TO HASBRO

The toymaker sticks with proven successes—or buys them

One day two summers ago, seven-year-old Darryl Bernstein lost interest in G.I. Joe. The event might have passed without notice, except that Darryl's father is Lawrence H. Bernstein, the Hasbro Inc. executive vice-president charged with keeping the four-inch-tall paramilitary hero in fighting trim. As Dad performed some hasty on-site market research, he got some crushing news. "Daddy," Darryl said, "you make boring toys."

Dad wised up. And in 1991, G.I. Joe went "toy-etic," as people who sell playthings for a living like to describe action toys that fly, shoot, and make considerable noise. All told, Bernstein overhauled 80% of Joe's line. Out went combat fatigues and in came spacesuits, jetpacks, and battle copters. Kids ate up the new look: After a scary three-year drop in sales, 27-year-old Joe should produce nearly \$120 million in revenues by Christmas, up slightly and well ahead of analysts' early expectations.

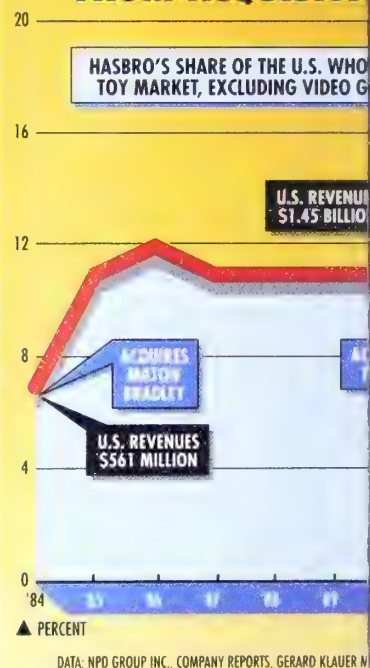
G.I. Joe's rejuvenation says much about why Hasbro, based in Pawtucket, R.I., is the world's biggest, most consistently successful toymaker. Simply put, Hasbro can teach old plush dogs—and dolls, and action figures—new tricks: In an industry that often relies on new-product pizzazz, Hasbro manages old products wisely.

STRAWBERRY SHORTCAKE. That's good, since Hasbro's product development efforts have been sadly ineffective. "You look at the record in the last five years, and they haven't had much," says Richard V. Sallis, senior vice-president at rival Playmates Toys Inc., distributor of the wildly successful Teenage Mutant Ninja Turtles toy lines. Hasbro, in fact, passed on a chance to license the Turtles. And it has achieved its poor record on new products despite a research budget 50% higher than that of archrival Mattel Inc. Since 1986, the lack of new-product excitement has meant slow domestic growth and stagnant profits.

But if you can't come up with your own toys to play with, you can buy somebody else's. This Christmas, Hasbro will enter the holiday fray with a wealth of new products, thanks to its recently

completed \$486 million acquisition of Tonka Corp. (chart). Besides picking up Tonka trucks, Hasbro added the Parker Brothers unit, maker of Monopoly, Milton Bradley division, whose board games already account for a chunk of U.S. profits. Parker Brothers had come to Tonka along with Kenner Products in a 1987 deal that crippled the company with debt and sapped its

A HELPING HAND FROM ACQUISITION



marketing strength. Even so, Kenner and Hasbro such past successes as Strawberry Shortcake doll and Barbie figures.

The purchase should add about \$100 million to Hasbro's \$1.5 billion of revenues, and profits should jump to about \$125 million, from \$89.2 million last year. But Hasbro is taking a \$59 million charge to cover consolidation costs.

Hasbro Chief Executive Alan G. Saks and his team hope to revive the company's languishing brands and turn them into long-running, G.I. Joe-like

Hassenfeld's goal is to get 70% of revenues from staple products. Unom-and-bust toys—Teddy Ruxpin, racy action figures, and the Tursteady sellers have lower manufacturing costs because they use the same molds from year to year. And sales are less volatile, shelf space is easier to come by: Retailers love pre-performers to balance riskier such cash-churning staples keep the company's gross margins the industry's at 53%.

TRUCKS. Tonka could be fertile ground for Hasbro. In an age when fun has moved over Nintendo Co.'s Game Boy, sales of Tonka's rugged die-cast trucks have plateaued at about \$70 million. But Hassenfeld and Bernstein figure they can recreate with trucks their success with Cabbage Patch Kids. When Hasbro acquired the line in 1989 along with its parent, Coleco Industries Inc., sales had dropped to about \$25 million, down from a 1985 peak of \$575 million. Hasbro



HASSENFELD: OVERHAULING TONKA

introduced new dolls with heavy advertising and quickly broadened distribution. Revenues tripled within a year.

With the trucks, Hasbro intends to invest in advertising to rebuild the Tonka brand. Perhaps more important in the long run is the age of budget-conscious parents, who seem to want to dust off a major seller from the trucks: their lifetime favorite, begun as a consumer promotion years ago but underplayed by Hasbro. "I can't wait to do trucks," Hassenfeld says.

Hasbro's other lines, Hassenfeld

figures more and better advertising, especially for such well-known names as Play-doh, Nerf, and the word game Boggle, should help a lot. Other Tonka products may be headed for the big toy chest in the sky, though. The Kenner division's once successful Ghostbusters line, for example, has been slided by the Ninja Turtle success, and sales are off 75% from their 1989 peak.

But analysts and competitors agree that Hasbro manages such disappearing acts with a deft touch. Hasbro checks weekly sales at hundreds of U.S. stores, assessing changing buying patterns for its entire product line. It can adjust manufacturing plans within weeks, or change the number of new items in the following year's line to reflect shrinking demand. That's how Hasbro makes money with My Little Pony, the line of horse figures that appeared in 1983 and reached \$100 million in sales in 1985. Eight years later—several lifetimes for such a fad—Hasbro should make \$4 million on sales of just \$20 million.

As Hasbro gets its "new" toys into shape, it may get a boost this Christmas from the absence of any megahit that would suck up parents' dollars. And Hasbro may even be getting more creative. Analyst Sean McGowan at Gerard Klauer Mattison & Co., among others, believes that Hassenfeld has encouraged innovation more than his brother and predecessor, Stephen, who died in 1989. Despite reduced research spending, three new lines—a walking puppy, some World Wrestling Federation figures, and a set of New Kids on the Block toys—made a total of \$70 million in revenues last year. And Bernstein is taking unaccustomed risks on licenses for the movie *Terminator 2* and on the character Steve Urkel from TV's *Family Matters*.

But the real money still lies in older brands, as Hasbro's rivals know. Playmates is giving face-lifts to 80% of its Turtles line in an effort to slow declining sales. Mattel does much the same with Barbie, its indefatigable fashion doll, and the aging line of Hot Wheels cars.

A question remains for Hasbro, though. If in-house creativity fails to produce enough long-term hits, will the biggest toymaker of them all run out of old reliables to buy? As toy retailers consolidate, all but the largest, best-financed manufacturers are being squeezed out. Some independents, such as loss-plagued Lewis Galoob Toys Inc. (box) remain, but they are getting scarce. Mattel, for example, just bought Aviva, a small independent maker of sports toys. Without a world of toymakers to choose from, Hasbro may need to keep G.I. Joe and his pals toyetic for another quarter-century.

By Keith H. Hammonds in Pawtucket, R.I.

TOYMAKER ON A TEETER-TOTTER

To get an idea of how skilled Hasbro is, consider the syndrome afflicting South San Francisco's Lewis Galoob Toys Inc. Baby Talk dolls pushed it to \$111 million in sales and a stock high of 18¾ in 1986, but sales plunged to \$67 million in 1987. Next, Micro Machines miniature vehicles propelled sales to \$228 million in 1989 before crashing last year, for a \$32 million loss on sales of \$127 million. Recent stock price: 5¼.



In June, the company's board accepted the resignation of CEO David Galoob, 42, son of the founders. Analysts speculate about a palace coup, citing David Galoob's reputation as a free spender on product development and marketing. He brushes aside such talk, saying the parting was "amicable." But his departure takes another toy company out of a family's hands and entrusts it to a professional chief—in this case, Mark D. Goldman, a 40-year-old MBA from the University of Chicago who until June was No. 2 man at Galoob.

ROLE MODEL. Goldman takes over at an uncertain moment. In January, the board hired Bear, Stearns & Co. to find a buyer or a partner. So far, none has turned up, and none probably will until the business stabilizes, says John G. Taylor, an analyst at L. H. Alton & Co.

Goldman's model for stability is Hasbro: "It was created methodically over a decade," he says. "With discipline, you can grow a smaller, volatile company into a larger, stable one." So Goldman wants some perennial lines of his own to produce \$30 million to \$60 million in annual revenues each. He is reorganizing Micro Machines, for example, around lines kids can collect, such as antique cars. And Baby Face dolls, with different facial expressions, will probably get some relatives.

The stock recently rose after a judge ruled the company could sell Game Genie, a device to enhance a player's moves in Nintendo games. The market for 8-bit Nintendo machines is dwindling, but Goldman thinks Genie is still good for well over \$10 million in sales this year. Hardly a blockbuster—but then Goldman would be happy with a few profitable plodders, not just successes that fall as fast as they rise.

By Maria Shao in South San Francisco

1	Exxon
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4	Ford Motor
5	IBM
6	Texaco
7	E I du Pont
8	Standard Oil (Ind.)
9	Standard Oil of Cal.
10	General Electric
11	GOULD
12	Atlantic Richfield
13	Shell Oil
14	Occidental Petroleum
15	U.S. Steel
16	Phillips Petroleum

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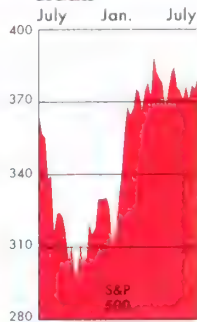
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Investment Figures of the Week

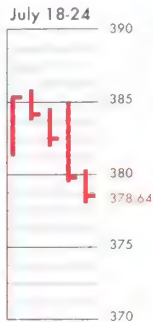
MARKET SUMMARY

A strong week in the financial markets. The Dow Jones Industrial Average surged 38 points on July 18, as investors bet on an upswing in the economy. But the market treaded a couple of days before the end of the week, as points on July 23 and on July 24. Earnings reports, and a drop in oil prices, contributed to the decline. Small and large companies joined in the decline. The market, particularly in the technology sector, was better.

STOCKS

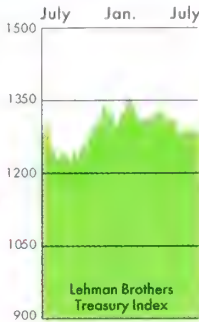


52-week change
+6.0%

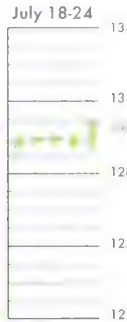


1-week change
-0.7%

BONDS

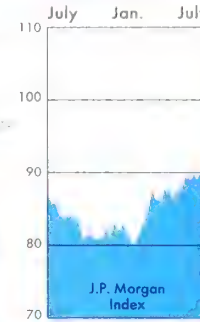


52-week change
+1.1%



1-week change
+0.8%

THE DOLLAR



52-week change
+1.6%



1-week change
-0.9%

MARKET ANALYSIS

	Latest	% change Week	% change 52-week
INDUSTRIALS	2966.2	-0.4	1.2
TECHNICALS (Russell 1000)	197.7	-0.8	6.8
COMPANIES (Russell 2000)	170.2	-0.7	4.0
FINANCIALS (Russell 3000)	210.0	-0.8	6.7

	Latest	% change (local currency) Week	% change (local currency) 52-week
FINANCIAL TIMES 100	2580.5	0.8	9.1
NIKKEI INDEX	23,297.5	1.0	-26.5
(TSE COMPOSITE)	3518.6	-0.7	-1.0

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.7%	5.8%	7.8%
30-YEAR TREASURY BOND YIELD	8.4%	8.5%	8.6%
S&P 500 DIVIDEND YIELD	3.3%	3.2%	3.3%
S&P 500 PRICE/EARNINGS RATIO	18.7	18.7	16.5

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 26-week moving average	373.3	371.3	Positive
Stocks above 26-week moving average	54.5%	57.7%	Neutral
Speculative sentiment: Put/call ratio	0.40	0.47	Neutral
Insider sentiment: Vickers sell/buy ratio	3.04	3.02	Negative

INDUSTRY GROUPS

WEEK LEADERS

	% change 4-week	% change 52-week
TECHNICALS	15.5	26.2
TECHNICALS	10.2	-9.1
TECHNICALS	9.8	31.3
TECHNICALS	9.3	-13.1
TECHNICALS	8.8	23.2

WEEK LAGGARDS

	% change 4-week	% change 52-week
TECHNICALS	-9.6	7.0
TECHNICALS	-5.3	1.9
TECHNICALS	-4.3	28.9
TECHNICALS	-3.8	17.2
TECHNICALS	-2.8	-13.0

Strongest stock in group

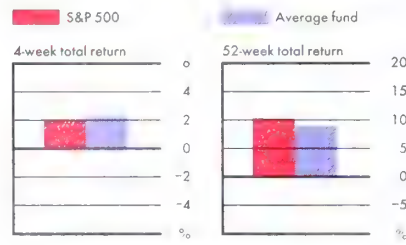
	% change 4-week	% change 52-week	Price
REEBOK	21.9	78.1	28 1/2
SCHLUMBERGER	14.6	3.3	66 5/8
FLEETWOOD ENTERPRISES	12.4	40.2	34
ECHO BAY MINES	16.4	-21.2	9 3/4
CROWN CORK & SEAL	9.7	32.1	83 1/4

Weakest stock in group

	% change 4-week	% change 52-week	Price
KAUFMAN & BROAD HOME	-26.5	0.0	10 3/8
ALBERTSON'S	-8.5	6.7	37 7/8
ROADWAY SERVICES	-8.3	38.5	49 1/2
LIZ CLAIBORNE	-8.4	34.8	42 1/8
EASTERN ENTERPRISES	-3.0	-8.8	24 1/2

MUTUAL FUNDS

	%	LAGGARDS	%
Four-week total return		Four-week total return	
CAPITAL DEVELOPMENT	10.6	AFUTURE	-6.3
NATIONAL INVESTORS	9.9	SFT EQUITY	-4.8
SERVICES GOLD SHARES	8.8	SFT ODD LOT	-4.3
52-week total return		52-week total return	
SELECT BIOTECHNOLOGY	55.9	STEADMAN OCEANOGRAPHIC TECHNOLOGY	-38.3
SELECT MEDICAL DELIVERY	52.1	BULL & BEAR SPECIAL EQUITIES	-34.7
SELECT HEALTH CARE	49.4	STEADMAN AMERICAN INDUSTRY	-29.5



RELATIVE PORTFOLIOS

Amounts at the present \$10,000 one year ago portfolio					
Figures indicate total returns	Treasury bonds	U. S. stocks	Money market fund	Gold	Foreign stocks
	\$10,917	\$10,766	\$10,602	\$10,205	\$9,202
	+0.24%	-0.16%	+0.11%	-0.56%	-0.36%

This page is as of market close Wednesday, July 24, 1991, unless otherwise indicated. Groups include S&P 500 companies only; performance and share prices are as of market close.

July 23. Mutual fund returns are as of July 19. Relative portfolios are valued as of July 23. A more detailed explanation of this page is available on request.

HOLD THE SAME STICK OVER ALL INSURERS

Insurance is supposed to be safe and dependable, if not a little boring. So when millions of Americans suddenly find themselves wondering if they can really count on their insurance companies for retirement and death benefits, something has clearly gone askew.

High anxiety is sweeping this country in the wake of several runs by policyholders and state takeovers of insurance companies. The present patchwork of state regulation of the insurance industry has left some policyholders protected and others holding the bag. The reality is that some states provide excellent oversight, and some do not. Some protect nearly all policyholders with financial safety nets, and others offer only promises (page 42).

The insurance industry needs uniform standards across the land—particularly when insolvency strikes—and that usually means federal regulation. But the savings and loan debacle has shown us that federal involvement is no panacea. Congress has no appetite to take on any further oversight, let alone make good losses in another financial industry. Any attempt to get Washington involved in regulating the insurance industry is likely to take years.

A better solution is for the National Association of Insurance Commissioners, the umbrella group of state insurance regulators, to force stronger capital standards on the industry. Insurers have been writing more investment-oriented products and making riskier investments. These need bigger cushions of capital to protect policyholders.

The NAIC also should enforce uniform rules for state insurance funds. At the moment, for example, 20 state insurance funds cover guaranteed-investment contracts, or GICs, one of the most popular products sold by the insurance industry

in the 1980s. All the other state insurance funds

Both uniform rules and stiffer capital requirements help the consolidation under way in the \$1.4 trillion insurance industry. A major reshuffling is taking place among the 2,300 life insurance companies in the U.S. as consumers and pension managers switch funds from weak to strong hands.

NO GUARANTEES. Corporations have a major role to play in insurance reform through their pension programs. They have moved away from defined-benefit to defined-contribution plans, moving financial responsibility for retirement onto the shoulders of their employees. Companies bought nearly \$15 billion worth of GICs in recent years and offered them in lieu of employee 401(k) pension accounts without clarifying the investment risk involved. According to employee-benefit surveys, some 65% of all pension money in 401(k) retirement plans is invested in GICs. Employees are now bringing lawsuits against their corporations to compensate them for losses from GICs that went sour. The employees are holding the bag after putting their retirement money in an investment vehicle promoted as "guaranteed." It's something of a shock for them to find out now that neither the insurance company issuing the GICs nor the employer actually guaranteed anything. Companies owe it to their employees to offer a wide variety of investment vehicles and clearly explain the degree of risk in each.

In an era of job uncertainty and mobility, where individuals are expected to take charge of their retirement, people need more information and more assurance about their insurance. It doesn't have to cost taxpayers hundreds of billions of dollars, either.

THE PLAYING FIELD IS LEVEL—SO PLAY

Look closely, and you can see that the foundation of a more prosperous U.S. economy is being slowly built. Inflation is down, labor costs are the lowest in the industrialized world, manufacturing productivity is up, exports are strong, and the trade gap is narrowing. Perhaps most important, U.S. business no longer is hobbled by a steeper cost of capital than its foreign competitors. For the first time in recent memory, financing costs are getting cheaper in the U.S. and more expensive abroad.

Economists who have looked into capital costs agree that the U.S. no longer is handicapped. By one measure, capital costs averaged 7.5% in the U.S. compared with 5.4% in Japan in the second half of the 1980s. But by the first half of this year, capital costs in the U.S. had dropped to 5.9%, while Japan's had risen to 6.1%. Declining interest rates and a strong stock market at home in contrast with rising rates and a weak, scandal-ridden exchange in Tokyo have combined to give the U.S. a significant investment advantage.

One troubling recent economic trend has been American anemic investment performance. U.S. business capital spending is just 12% of gross national product compared with about 22% of GNP for Japan. Much has been made of Japan's management savvy as it became the world's most feared competitor in the 1980s, but its low cost of capital also played a major role. Japan's willingness to invest in the long run and America's obsession with the short term may have largely reflected different capital costs rather than cultural preferences.

The decline of U.S. capital costs vis-à-vis those of its trading partners has removed one of the last and most significant constraints on U.S. capital spending. And relief has come at a time when opportunities and competitive pressures in the global market and slow labor-force growth at home make increased investment essential. America's future prosperity rests on how forcefully U.S. business responds to this promising reversal of fortune.

BusinessWeek

AUGUST 12, 1991

A MCGRAW-HILL PUBLICATION

\$2.50

PERSONAL COMPUTERS

THE COMING DECADE

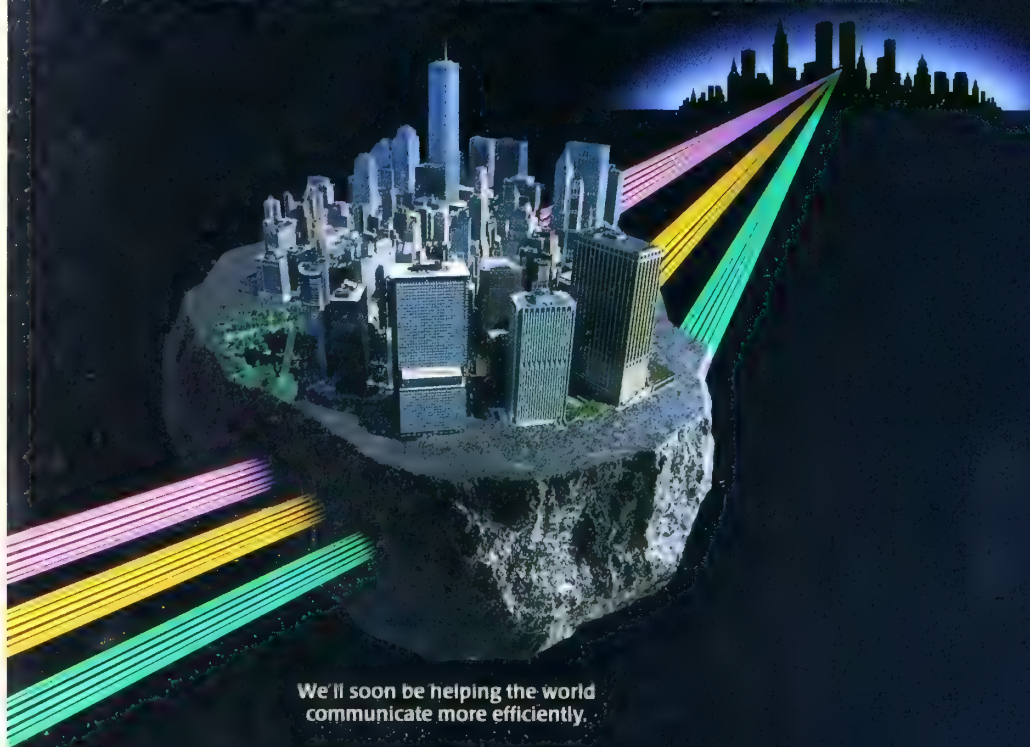
In the 10th anniversary of
IBM's PC, the industry is
in turmoil. Will IBM and
Apple, working together,
dominate? What
technology will be hot?
How will we use PCs in
the year 2000?



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And the power to find
the information you're looking for
in 0.3 seconds.



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title of every book in every library in North
ica.

another presents an entire encyclopedia to
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information is accessed in 0.3 seconds,
urrent industry benchmark. And reliability is
ed, in part, by new technology which
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working on a lot of bright ideas.

*US\$3,480 million; net R&D expenditures for the year ending March 31, 1991
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*For more information about the CD-ROM systems, call toll-free
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Macintosh computers
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It isn't a shortage of thinking, inspiration or motivation that prevents people from achieving their goals.

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Personal computers were supposed to streamline the mundane chores and monotonous routines so that we could concentrate on solving problems and moving ahead. What happened?

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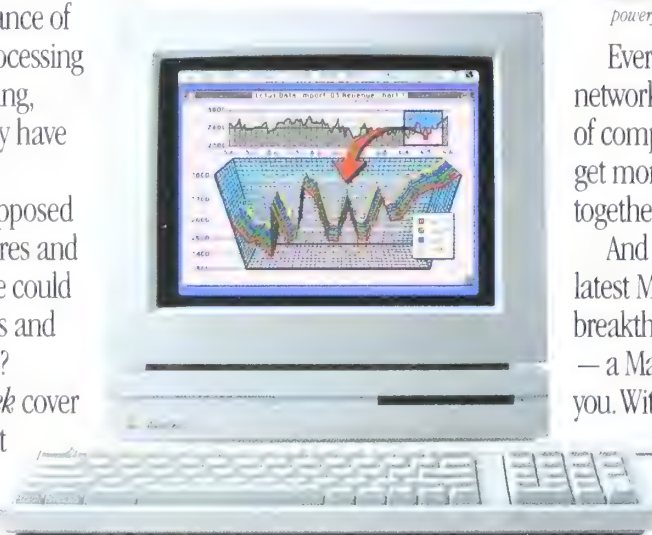
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network into less work and
company into more of a t

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And get your hands on the power you buy a personal computer for in the first place. The power to be your best.



Work less.



System 7 for Macintosh. 



THE BATTLE FOR YOUR LIVING ROOM: PC MAKERS WILL TRY TO WOO ORDINARY CONSUMERS WITH SYSTEMS THAT TIE INTO VIDEO AND CDs

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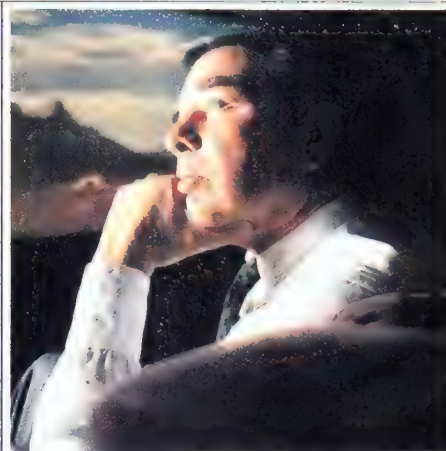
One slip could send the economy into double dip



MY PEOPLE ARE IN A HURRY:
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DISCUSSES POVERTY, FREE TRADE,
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MORE TOP EXECs ARE BEING HIRED
FROM OUTSIDE, THANKS TO THEIR
GREATER WILLINGNESS TO CUT STAFF
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FACES HIS TOUGHEST MISSION YET—
WRINGING ENOUGH REVENUE FROM A
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The muck from BCCI is flowing into the White House

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More men are revamping their wardrobes by changing neckwear

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The commercial space-launch business has too many companies with too many rockets chasing too few payloads

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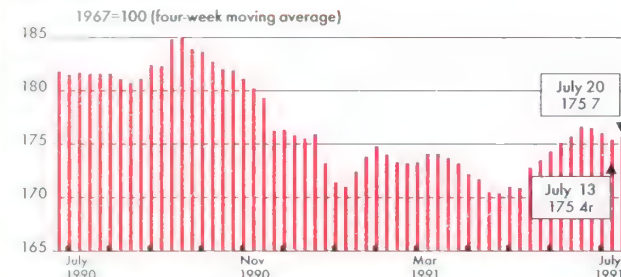
78 EDITORIALS

The Baby Bells still need a guardian
Fair play on the Tokyo Exchange
Banks shouldn't ditch small business

BusinessWeek Index

PRODUCTION

Change from last week: 0.2%
Change from last year: -3.2%

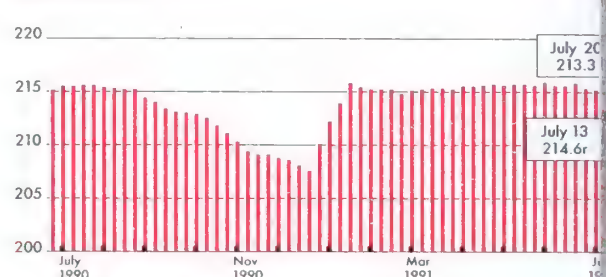


The production index rose for the week ended July 20. After seasonal adjustment, a large increase in electric-power output accounted for most of the gain, as record heat over much of the nation caused unusually heavy demands on utilities. Output of trucks, paper, paperboard, lumber, crude-oil refining, and rail-freight traffic also rose. Production of steel and coal fell, and auto output was unchanged. Before calculation of the four-week average, the index jumped to 179.3, from 175.4.

BW production index copyright 1991 by McGraw-Hill Inc.

LEADING

Change from last week: -0.6%
Change from last year: -1.1%



The leading index declined in the week ended July 20. Stock prices fell. The growth of materials prices continued to slow down, as did real estate loans. Initial claims for unemployment insurance rose. On the plus side, bond yields declined, and the growth rate of the M2 money supply picked up. Large-business failures were not available. Before calculation of the four-week average, the leading index fell to 210.9, from 213.3 in the previous week.

Leading index copyright 1991 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (7/27) thous. of net tons	1,668	1,600#	-9.6
AUTOS (7/27) units	80,526	91,440r#	-16.8
TRUCKS (7/27) units	59,228	70,142r#	-23.3
ELECTRIC POWER (7/27) millions of kilowatt-hours	67,382	66,980#	7.0
CRUDE-OIL REFINING (7/27) thous. of bbl./day	13,842	13,798#	-3.6
COAL (7/20) thous. of net tons	19,372#	18,042	-5.3
PAPERBOARD (7/20) thous. of tons	785.2#	743.8r	2.2
PAPER (7/20) thous. of tons	736.0#	669.0r	-1.1
LUMBER (7/20) millions of ft.	556.9#	503.2	14.5
RAIL FREIGHT (7/20) billions of ton-miles	19.4#	18.7	-6.3

Sources: American Iron & Steel Inst., Ward's Automotive Reports, Edison Electric Inst., American Petroleum Inst., Energy Dept., American Paper Inst., WWPA¹, SFPA², Association of American Railroads

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (7/31)	138	137	149
GERMAN MARK (7/31)	1.74	1.73	1.59
BRITISH POUND (7/31)	1.69	1.70	1.86
FRENCH FRANC (7/31)	5.93	5.89	5.34
CANADIAN DOLLAR (7/31)	1.15	1.15	1.15
SWISS FRANC (7/31)	1.52	1.51	1.35
MEXICAN PESO (7/31) ³	3,022	3,017	2,879

Sources: Major New York banks. Currencies expressed in units per U. S. dollar, except for British pound expressed in dollars.

PRICES

	Latest week	Week ago	% Change year ago
GOLD (7/31) \$/troy oz.	362.850	366.000	-2.1
STEEL SCRAP (7/30) #1 heavy, \$/ton	90.50	89.00	-24.3
FOODSTUFFS (7/29) index, 1967=100	205.8	198.7	-7.9
COPPER (7/27) ¢/lb.	103.6	103.2	-18.7
ALUMINUM (7/27) ¢/lb.	58.9	60.0	-18.8
WHEAT (7/27) #2 hard, \$/bu.	2.99	2.86	-2.0
COTTON (7/27) strict low middling 1-1/16 in., ¢/lb.	70.00	70.91	-12.2

Sources: London Wed. final setting, Chicago mkt., Commodity Research Bureau, Metals Week, Kansas City mkt., Memphis mkt.

#Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (7/26) S&P 500	380.57	382.95	0.6
CORPORATE BOND YIELD, Aaa (7/26)	8.97%	8.99%	0.2
INDUSTRIAL MATERIALS PRICES (7/26)	96.7	97.8	1.1
BUSINESS FAILURES (7/19)	NA	354	NA
REAL ESTATE LOANS (7/17) billions	\$400.5	\$403.7	0.8
MONEY SUPPLY, M2 (7/15) billions	\$3,397.2	\$3,389.6r	0.2
INITIAL CLAIMS, UNEMPLOYMENT (7/13) thous.	425	395	7.6

Sources: Standard & Poors, Moodys, Journal of Commerce (index: 1980=100), Dun & Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. CIBCR seasonally adjusts on business failures and real estate loans.

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
MANUFACTURERS' INVENTORIES (June) billions	\$380.3	\$381.9r	0.4
MANUFACTURING SHIPMENTS (June) billions	\$239.0	\$238.3	0.3
PERSONAL INCOME (June) annual rate, billions	\$4,802.6	\$4,780.0r	0.5
NEW HOME SALES (June) annual rate, thous.	525	489	7.3

Sources: Commerce Dept.

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (7/15)	\$857.5	\$856.9r	0.1
BANKS' BUSINESS LOANS (7/17)	304.4	306.5r	0.7
FREE RESERVES (7/24)	422	293r	43.7
NONFINANCIAL COMMERCIAL PAPER (7/17)	147.5	148.1	0.4

Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed in two-week period in millions).

MONEY MARKET RATES

	Latest week	Week ago	% Change year ago
FEDERAL FUNDS (7/30)	5.75%	5.74%	8.9
PRIME (7/31)	8.50	8.50	10.0
COMMERCIAL PAPER 3-MONTH (7/30)	5.96	6.00	7.0
CERTIFICATES OF DEPOSIT 3-MONTH (7/31)	5.92	5.94	7.0
EURODOLLAR 3-MONTH (7/27)	5.98	6.00	8.0

Sources: Federal Reserve Board, First Boston

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THE LAST THING PRIVATE SCHOOLS NEED IS PUBLIC MONEY

Although I appreciate Gary Becker's acknowledgment that competition will strengthen our educational system, I must disagree with the voucher solution proposed by President Bush and endorsed by Becker ("Public funds for religious schools would be no sin," Economic Viewpoint, July 15). In the end, it will only serve to weaken the educational system by bringing more of it under the stifling—albeit "politically correct"—umbrella of the federal government. I hope that patrons of private schools and home-schoolers will have the good sense to not accept public money for their educational efforts if it is offered. Although they must currently pay twice for education, at least they have not yet abdicated their right and responsibility for education to the state. The constitutional, logical, moral, and economical way to achieve educational reform is through total privatization.

Victor Mote
Colorado Springs, Colo.

BEAT THE JAPANESE? GET 'EM TO IMITATE US

In the past year, BUSINESS WEEK has entertained many proposals on leveling Japan's trade surplus. I have five suggestions for reducing the competitiveness of Japanese industries: First, export MBAs to Japan to get them on the path of short-term, numbers-oriented, shallow thinking. Second, send lawyers. Next, convince Japanese executives that their salaries should match those of Americans. Prove that only people who earn less than \$60,000 per year should be held accountable for their performance. By getting Japanese executives to take the same salaries Americans get, we could demoralize Japanese workers while dramatically raising operating costs for Japanese corporations. Fourth, get Japanese executives into the habit of laying off the lowest-paid workers while giving themselves huge raises, whether the corporation is profitable or not. This fine American tradition could help Japanese workers to be as motivated as most

Americans are to help their companies' long-term growth and strength. Finally, once Japan's productivity, long-term planning, and innovation are reduced to American big-business levels, we can work on eliminating other barriers.

Donald Sacz
Elizabeth, N. J.

THE GREENING OF NEW ENGLAND ELECTRIC

Regarding "Making clean energy sweeter to utilities" (Environment, July 15): Never did I contend that the Massachusetts plan for use of environmental externality factors for utility resource planning is "full of holes." The Massachusetts plan represents, in its most basic form, a simple statement that environmental issues matter and ought to be included in utility resource planning. We at New England Electric wholeheartedly agree with that concept.

David L. Holt
Director of Engineering
New England Electric System
Westborough, Mass.

CALPERS' 'SURPLUS' IS NOT FOR PETE WILSON TO PLAY WITH

In the article "Pete Wilson should keep his hands off CalPERS" (Editorials, July 1), you have taken a correct stance. Someone should point out to Governor Wilson that the funds in CalPERS do not belong to the State of California, to him, or to the state legislature: They belong to current retirees and employees. The oft-cited "surplus" of \$1.6 billion is the result of above-average investment performance. Prudent investment requires it be held as a reserve against likely future below-average performance.

Tony Lima, Professor of Economics
California State University
Hayward, Calif.

WHY THE GOVERNMENT ISN'T UP TO HANDLING HEALTH CARE

As CEO of a major manufacturing company struggling with the rapidly increasing cost of health care, I have a problem with Robert Kuttner's reasoning and that of the Democratic sponsors

BUSINESS WEEK
AUGUST 12, 1991 ***3226
ISSN 0007-7135



Published weekly except for one issue in January, by McGraw-Hill Inc. Founder: James H. McGraw (1860-1948). Executive, Editorial, Circulation, and Advertising Offices: McGraw-Hill Building, 1221 Avenue of the Americas, New York, N.Y. 10020. Telephone: (212) 512-2000. Domestic Telex: 127560, International Telex: 232965. Cable: McGraw-Hill New York, TWX: 710-351-4879. U.S. subscription rate \$44.95 per year, 2 years, \$74.95; 3 years, \$99.95. Single copies, \$2. Write for rates in other countries. Business Week Subscriber Services: 1-800-635-1200.

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European Circulation Center, McGraw-Hill House, Maidenhead, Berks England Telephone: (0628) 23431, Telex: 48640.

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The Energy To Change



Readers Report

"long-awaited national health insurance bill" ("A second opinion on the Democrats' health plan," Economic Front, July 1).

we must recognize that the science of medicine is advancing at a breathtaking rate that is far outstripping society's ability to face the moral and ethical questions that exist on the edge of medicine. For instance, we have the ability to save severely injured babies at enormous cost and with less than ideal results, such as long-term handicaps. Is it wise to ethically try to save these babies? Who makes the decision? Just a few years ago, we didn't have the problem; they simply didn't survive.

And, we must recognize that we Americans have been raised to think of health as a "right." We believe we're lucky enough to have medical coverage supplied by our employer, our employer's obligation, and it shouldn't cost us anything. We believe we should all have unlimited access to the best care available, and when we have that right, we have the absolute right to expect perfect results. If we don't get it, we should be dissatisfied by somebody—usually

CORRECTIONS & CLARIFICATIONS

In a table rating the 15 biggest insurers ("The rating game: When A+ equals C-," Cover Story, Aug. 5), we misstated the BUSINESS WEEK composite index for New York Life; the correct number is 1.2. We erroneously listed a Duff & Phelps rating for Northwestern Mutual Life; the agency does not rate Northwestern Mutual. Northwestern also received the highest BW rating, a 1.2.

The caption for the photo of silicon-based aerogels (Table of Contents, July 29) should have said the aerogels were developed at Lawrence Livermore National Laboratory.

through the plaintiff's bar and somebody else's liability insurance.

Can a "single payer" (i.e., the federal government) answer these difficult questions? Nothing in recent history should give us much confidence that it can.

We will, as a people, have to individually pay much, much more for health care than we have in the past. If we pay through higher premiums, larger deductibles, etc., we will, though it will hurt,

manage our health care costs better than if some faceless bureaucracy does it for us.

John W. Norris Jr.
Chairman and CEO
Lennox International Inc.
Dallas

DON'T BLAME FOREIGN-CAR BUYERS FOR DETROIT'S SCREW-UPS

Regarding the letter "Are diehard Toyota owners killing Detroit?" (Readers Report, July 22): It burns me up that Michael Weiner blames foreign-car buyers for the financial difficulties of the states and for individuals who are out of a job. The primary culprit in the auto industry is American automobile manufacturers. There wouldn't have been a mass exodus from American cars if their manufacturers offered quality and cared about their customers.

Stephen A. Snyder
Reisterstown, Md.

Letters to the Editor should be sent to Readers Report, Business Week, 1221 Avenue of the Americas, New York, N.Y. 10020. Fax: (212) 512-4464, Telex: 12-7960, Intl. 4998204. All letters must include an address and daytime and evening telephone numbers. We reserve the right to edit letters for clarity and space.

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BOOK BRIEFS

TRUMPED! THE INSIDE STORY OF THE REAL DONALD TRUMP—HIS CUNNING RISE AND SPECTACULAR FALL

By John R. O'Donnell with James Rutherford
Simon & Schuster • 348pp • \$21.95

NO ART TO THE DEALS

Last December, a lawyer representing Donald Trump visited John R. O'Donnell, who until April, 1990, had been president of Trump Plaza, the mogul's only successful Atlantic City casino. O'Donnell was writing a book about his experiences. The lawyer told O'Donnell that if he published the book, Trump would release derogatory (and false, says O'Donnell) information about him. O'Donnell kept on writing.

Considering the ridicule The Donald has suffered of late, O'Donnell's *Trumped!*, while sharply critical, lands no mortal blows. Yet Trump had reason to worry: The book's portrayal of Trump the Manager is often devastating. It reinforces the the-

ory that Trump's fortune, now depleted, derived more from rising real estate prices than from business acumen.

O'Donnell sees Trump as erratic and indecisive, lurching unpredictably from strategy to strategy—in part because of a limited attention span and a propensity to believe the last person he spoke to. Trump, he writes, couldn't "sort his thoughts out on a daily basis, let alone provide long-term corporate direction."

Although Trump loves deals, he had little interest in business minutiae, according to O'Donnell. While much of his net worth was tied up in gambling, for instance, he made no effort to learn how casino games work. The only time he saw his boss happy, O'Donnell says, was ringside at boxing matches.

The book's most arresting section discusses the opening of the Taj Mahal in April, 1990. The Taj, it says, "was a disaster area of muddled and insufficient planning." Most calamitous was a breakdown in slot-machine operations. For a long time, Trump refused to even believe there was a problem. When gaming officials shut

down most of the slots for several days, he became nearly hysterical, castigating most of his executives, including O'Donnell, who soon resigned.

The Trump described here is surely a hopelessly inept manager, you finish the book feeling almost sorry for the guy.

BY CHRIS WE



TRUMP: ERRATIC—AND NO MANAGER

THE PACIFIC RIM ALMANAC

Edited and written by Alexander Beshar
HarperCollins • 824pp • \$39.95/\$19.95

PACIFIC POTPOURRI

Readers should approach this sprawling volume in much the way they might explore the Pacific Rim itself—little by little.

The book is a compilation of short pieces, mostly from West Coast and Hong Kong publications. It is loosely organized around such topics as lifestyle, marketing, trade, money, and ecology.

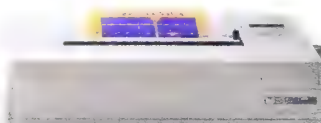
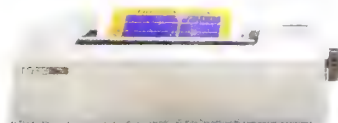
Most valuable are the insights into lifestyles and marketing, which reflect Asia's diversity and amazing rate of change. Bangkok has multiplex theaters. Young people in Singapore listen to a spicy radio station from nearby In-

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aiwanese yuppies buy \$7 cups of . In Hong Kong, Marlboro is the advertiser; in Singapore, McDon- in Thailand, Colgate-Palmolive. andful of articles will stimulate experienced Asia hands. One ar- that in response to the creation of th American free-trade zone and e 1992, Asians must regionalize industries to remain competitive. er suggests that a lack of labor ty could emerge as the region's es' heel. Alas, these more sophisti- articles are short and inconclusive. almanac also often exhibits a dis- ting "New Age" sensibility. San isco-based Beshner and some con- sors see the region's cultures, busi- nterests, and peoples headed for n." Everything from Japanese fi- to Balinese music to Malaysian -analysis is lumped together. One suggests that Japan will tune in feedback and channeling, and that rnia and Japan will join in a "wave rnsformative social consciousness." then, those sections speak vol- about California, a distinctive part Pacific Rim. It is the *Almanac's* to alternately inform and provoke makes it worth owning. Think of it West Coast concoction: Asia Lite.

BY WILLIAM J. HOLSTEIN

BY BUSINESS WEEK WRITERS

BROKERS, BAGMEN, AND MOLES: FRAUD AND CORRUPTION IN THE CHICAGO FUTURES MARKETS

By David Greising and Laurie Morse
John Wiley & Sons • 337pp • \$24.95

POSING IN THE PITS

When you think of undercover cops, you usually picture police posing as fences, drug buyers, prostitutes, or their customers. This book tells of a sting of a different sort. For more than two years, four agents from the Federal Bureau of Investigation worked in the commodity futures trading pits at the Chicago Board of Trade and the Chicago Mercantile Exchange, trying to nab traders cheating customers. Their investigation became public on the night of Jan. 17, 1989, when the agents, accompanied by government lawyers, began knocking on the doors of traders and brokers caught in the trap.

The FBI men faced a fascinating challenge. None of them had ever been a trad-

er, and all had to learn the grueling floor-trading business well enough to pass as credible neophytes and draw seasoned professionals into their confidence. They also had to understand the rules well enough to know when the law was broken. By day, they traded with government money—often not too successfully. By night, they transcribed incriminating conversations picked up by hidden tape recorders and made notes of what they had learned.

Authors David Greising, a Chicago correspondent for BUSINESS WEEK, and Laurie Morse, of Knight-Ridder Financial News, place the scandal in historic context. Impropropriety, they tell us, isn't new to the pits. They examine the cliquish power structure at the exchanges and the lax regulatory environment that let lawlessness flourish.

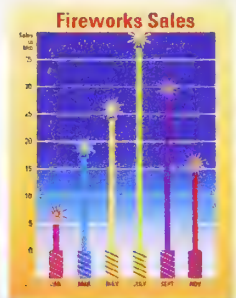
The story hasn't ended. Of the 48 people indicted, 22 pleaded guilty and 13 have been convicted. Most traders were acquitted of at least some charges—hardly a resounding success for the government. Still, this recounting provides a look inside a wild, little-understood business.

BROKERS, BAGMEN & MOLES



DAVID GREISING & LAURIE MORSE

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THE HIGH COURT DEBATE ISN'T HIGH—OR BROAD—ENOUGH

BY GARY S. BECKER



The Supreme Court has widened its role in the past 40 years. But the confirmation process is still limited to just a few highly charged issues.

President Bush has stated that Clarence Thomas, his nominee to the Supreme Court, is the best person for the job. Yet everyone knows that not only Thomas' race but also his views on affirmative action, abortion, and other politically sensitive questions were decisive considerations for Bush.

The Senate Judiciary Committee will subject Thomas to a close and partisan examination, although the proceedings will be cloaked in highfalutin language: Does the candidate respect precedent? Does he believe in privacy and fairness? Such questions will generate prolonged hearings that may seem tedious to many people and will certainly prompt objections from the White House that the Senate is badgering the witness. Indeed, extensive hearings prior to confirmation were not expected by the Founding Fathers, who anticipated that the highest court would simply interpret the Constitution. But the impact the court has come to have on Americans has made the modern confirmation process inevitable.

The Supreme Court was much less important in the 19th century and the first two decades of this one—when governments were much smaller. With the vast expansion of federal and state legislation, issues touching on all aspects of our lives are now brought before the court. Since the Constitution is vague on many subjects—such as due process—and since federal and state legislation is often ambiguous, it was unavoidable that the highest court would emerge as a de facto legislative and regulatory body with enormous influence. Constitutional law itself became an important subject in law schools only during the 1930s.

To reduce the capacity of what is, in effect, an unelected upper chamber to deviate for prolonged periods from the wishes of the majority of voters, I proposed a constitutional amendment that would substitute a fixed term—possibly renewable—for the present lifetime tenure of judges (BW—Sept. 3, 1990). Such a change would help weed out senile and incompetent judges and those who get out of touch with public opinion.

FAULTY FORUM? Obviously, such a radical step is not likely to be taken soon. The confirmation hearings will continue to provide the only public forum to consider the qualifications, record, and philosophy of nominees such as Clarence Thomas who, if approved, will sit on the bench for a long time. Since 1950, the Senate has rejected several nominees: not only Robert H. Bork but also Nixon's nominees Harold Carswell and Clement Haynsworth. The Senate also defeated Lyndon B. Johnson's attempt to elevate Abe Fortas to Chief Justice.

Presidential nominations are greatly influ-

enced by expectations about who can get confirmed. The intellectual caliber of certain recent appointments to the Supreme Court has been rightly criticized, but it is clear that some professors and judges who have made impressive contributions to legal thought, such as Richard A. Posner and Frank H. Easterbrook of the U.S. Court of Appeals in Chicago, as well as Robert Bork, do not have a good chance of gaining approval from the present Senate. They are deemed too conservative. Similarly, liberals such as Laurence H. Tribe of Harvard University probably would not be approved by a conservative Senate.

Unfortunately, the political nature of the hearings means that the issues dear to well-organized interest groups with good access to the media are overemphasized relative to questions of greater significance. Pressure from vocal groups is a major reason why views on abortion are considered a litmus test of a candidate's qualifications to serve on the court. Such emotional controversies get attention, but they have less impact on most people than crime—which accounts for over one-quarter of all cases decided by the court—the regulation of business, employee rights, and other matters decided by the court.

LIP SERVICE. One important business issue concerns when federal legislation should preempt local laws. The chemical industry is unhappy with a June ruling by the court that federal regulations governing pesticide use do not preclude additional local controls. The explosion in large punitive-damage awards has led the insurance industry and trade groups to seek court protection with the claim that they have been deprived of due process. But the top court has not yet discovered constitutional constraints on the size of damages.

Liberal groups question whether Thomas and other recent nominees have sufficient respect for legal precedent. This lip service to precedent sounds like political sour grapes caused by unhappiness over recent reversal of court rulings on criminal procedure from the 1960s and early 1970s. Yet the Warren Court overthrew precedents that had guided criminal procedures for over a century. The present court has not been inclined to overthrow earlier decisions on business and labor issues where precedent does help plan for the future by stabilizing the legal environment.

The Supreme Court will continue to exert a powerful influence on economic and social issues as long as governments affect all aspects of life. It is only proper that confirmation hearings probe a nominee's views on many questions far removed from legal training and legal doctrine.

GARY S. BECKER IS UNIVERSITY PROFESSOR OF ECONOMICS AND SOCIOLOGY AT THE UNIVERSITY OF CHICAGO



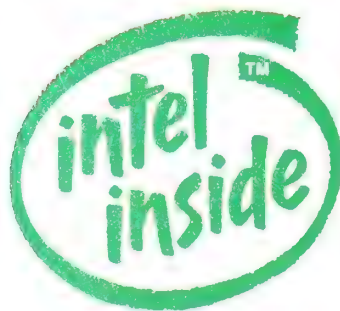
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BY MICHAEL J. MANDEL

SOME FORMER U.S. WEAKLINGS FLEX THEIR MUSCLES ABROAD

High-flying commercial airliners and other sophisticated symbols of America's export prowess have gotten most of the publicity, but the export boom is quietly spreading to the less glamorous parts of manufacturing as well. Overall, manufactured exports in the first five months of 1991 were 8.3% higher than in the comparable period a year earlier. More important, some of the biggest percentage gainers are industries that just a few years ago looked as if they would be overwhelmed by foreign competition.

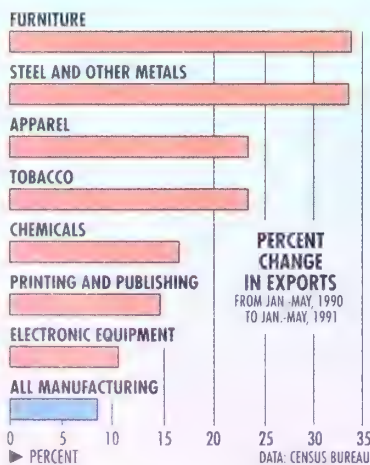
Heading the export growth list, with yearly gains exceeding 30%, are the furniture and primary-metal industries, in-

industrial machinery showed a meager 3.1% increase in exports.

Part of the new competitiveness in these four industries comes from lower wages. For example, steel and other metal makers are paying 16% per hour less than they were in 1982, in real terms. And in the past year, inflation-adjusted wages in the furniture and apparel industries have fallen by 1.4% and 1.9%, bigger declines than in the rest of manufacturing. Moreover, they're still pruning workers, even with their newfound surge in exports. Over the past year, furniture, metals, and electronics companies have recorded job losses exceeding 5.5%, more than the 4.3% drop for the entire manufacturing sector.

The recent export successes show that U.S. manufacturing is becoming more competitive across the board, and not just in a couple of high-tech industries. If this trend continues after the recession is over, it may be manufacturing, and not the service sector, that becomes the job machine of the 1990s.

THE EXPORT BOOM'S SURPRISING LEADERS



cluding the hard-pressed steelmakers (chart). Also showing a big export rise were the apparel and electronic-equipment industries. All four of these groups were nearly swamped by the import tidal wave of the late 1970s and early 1980s. Indeed, they have been among the biggest contributors to the persistent U.S. trade deficits.

So it's good news for U.S. competitiveness that these industries are making inroads overseas. True, the U.S. is still importing far more than it's exporting in these sectors, but their trade deficit has been reduced by 15% over the past year. Most of the shrinkage has come from strong growth in exports, rather than decreases in import demand induced by the recession. By comparison, aircraft exports rose by only 5.7%, and

THE ECONOMY HAS A CASE OF THE SUMMERTIME BLUES

A string of weaker-than-expected economic statistics, such as stagnating consumer confidence and the recent drop in durable-goods orders, have given the impression that the recovery may be faltering.

But economic bulls take heart. The apparent sluggishness may just be a case of the summertime doldrums, report economists Robert Giordano and Edward McKelvey of Goldman, Sachs & Co. They calculate that from 1984 to 1989, economic growth in the summer months—July, August, and September—was on average 30% slower than during the rest of the year, even after the government adjusted the numbers for seasonal variations. Business investment in plants and equipment, in particular, has usually been anemic in the summer. Even employment growth lags somewhat in those months. For example, in 1989, nonfarm payrolls in July, August, and September grew at a 1.5% annual rate, compared with 2.1% for the rest of the year.

Giordano and McKelvey suggest that the seasonal lull may reflect vacations as well as plant retoolings and other maintenance activities that are usually done during the slow summer months. So if the same pattern holds true this year, the normal hot-weather torpor may be hiding the gathering strength of the economic recovery.

FINALLY, A LITTLE SPARK IN THE SERVICE SECTOR

There's new evidence that the struggling service sector has turned the corner and joined manufacturing in recovery. According to a recent report from the Coalition of Service Industries, a Washington-based trade group, the service sector expanded in June for a third consecutive month. Based on such indicators as air-passenger miles, number of hospital admissions, trade volume, stock exchanges, and hours worked, the coalition's index of service-sector output rose by 0.2% in June. That's far slower than the 0.7% gain reported for industrial production in the same month, but it's still enough to bring production services back to the pre-recession level of June, 1990.

More important, all parts of the service sector are showing gains, according to the coalition's figures. That includes finance, retail trade, and even government. With the service sector in a plus column, the odds are rising that the recovery will turn out to be earnest.

U.S. WORKERS SUFFER FROM A TIME-OFF GAP

Companies in the U.S. offer their workers much less time off than most of their foreign competitors, according to a new report by Hewitt Associates, an employee-compensation firm in Illinois. Generally, an employee in one year of service gets only two weeks of paid vacation in the U.S., Canada, and Japan. By comparison, the same worker in Sweden, Denmark, Brazil, Austria, by law, can relax with 30 paid days off. And companies in Germany, Britain, France, and Spain are required to give 18 days or more of vacation to almost all their employees.

The vacation gap between the U.S. and the rest of the world does narrow as U.S. workers build up seniority, reports Mark S. Allen, an international compensation consultant at Hewitt. A typical U.S. worker with 25 years of service at one company, reports Allen, will get five weeks of vacation. However, because U.S. workers switch employers often during their working years, most will find themselves making do with far fewer days off than their foreign counterparts.

THE SLIP COULD SEND THE ECONOMY TO DOUBLE DIP

The recovery's durability is fast becoming a hot topic among economists. The double-dippers, who think the economy will slide back into recession, are taking the debate, facing off against the broad majority of forecasters who expect a sustained, if modest, upturn. The latest data provide ammunition for both sides, but one thing is increasingly clear: The recovery may be so fragile that the slightest policy mistake or external shock could knock it off course.

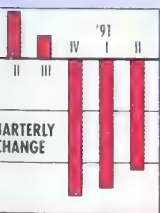
Some economists deny that a recovery is in place. The Commerce Dept.'s chief forecasting tool, its index of leading indicators, rose 0.5% in June. It was the fifth consecutive increase. And the index of coincident indicators, which tracks the economy's current path, rose 0.3%. That was the third consecutive increase, strongly suggesting that the recession ended around March or April.

However, even that far into recovery, the data have not yet certified the upturn's staying power. The Commerce Dept. reported that inflation-adjusted gross national product grew a scant 0.4% in the second quarter. The gain was below the general expectation and added at odds with the upbeat tone of some of the recent monthly numbers. Moreover, the GNP report entered little hope for much future strength.

PUT IS TO RISE RE THIS QUARTER

The GNP data did suggest that the best thing the recovery has going for it is lean inventories—perhaps too lean. Recessions always result in an inventory liquidation, and this downturn was no different. Inflation-adjusted stockpiles fell by \$21.2 billion in the second quarter, following declines of \$25 billion in the first quarter and \$18 billion in the fourth quarter (chart).

ING LIQUIDATION INVENTORIES



IN BILLIONS OF 1982 DOLLARS
DATA: COMMERCE DEPT.

at's because many businesses were caught short by a spring pickup in consumer spending, so they are cranking output to make sure stockpiles are sufficient to meet demand. In manufacturing, for example, inventories fell 0.4% in June, while shipments rose 0.3%. And

during the second quarter, factory stockpiles shrank by 1.5%, as shipments jumped 4.5%. That's one reason industrial production has been rising in recent months.

Those production gains, led by car output, should continue this quarter. U.S. inventories of cars and light trucks, both domestic and imported, dropped to a 34-month low on June 30, according to *Ward's Automotive Reports*, and Detroit is set to increase third-quarter output by 25%, seasonally adjusted. Economists estimate that such a fillip, taken alone, could boost the quarter's rate of growth in real GNP by two percentage points.

Double dips have occurred in past recessions mainly because businesses did not cut their inventories fast enough. An unwanted accumulation in the middle of past downturns, which boosted GNP, had to be liquidated, which later pulled GNP down again. But right now, extremely thin inventories bode well for the third quarter.

CONSUMERS MAY HAVE BLOWN THEIR WAD

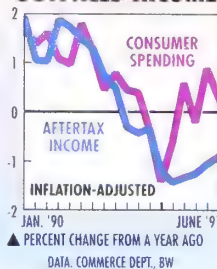
However, if this recovery is going to falter, the culprit is more likely to be weak demand that will short-circuit the need for businesses to pump up their production. On that front, a 1.4% drop in June factory orders, along with a sharp 1.1% decline in unfilled orders, raises some worry. Last quarter's GNP report wasn't very encouraging, either. Despite a big rise in consumer spending, overall demand didn't grow at all.

Consumer spending posted the strongest showing of any sector last quarter, as households lifted their inflation-adjusted outlays at an annual rate of 3.6%. However, that was three times faster than the 1.2% rise in aftertax income. Outlays are outpacing household earnings (chart), resulting in a drop in the saving rate last quarter to a paltry 3.7% of income.

In addition to exceptionally low savings for the early stage of a recovery and weak income growth, consumers are still burdened by heavy debts. Installment credit as a percentage of disposable income has declined somewhat, but remains high. The ratio of mortgage debt to income is at a record high. And the interest cost of servicing all this debt is also at record levels in relation to income.

It's little wonder that consumers don't feel excited about the recovery. The Conference Board's index of consumer confidence dipped slightly in July, to 77.7 from 78 in June. The index has remained essentially un-

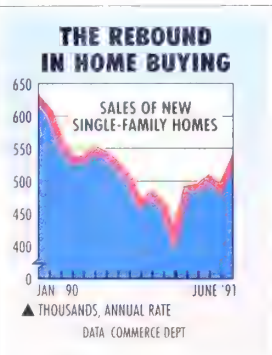
SPENDING FAR OUTPACES INCOMES



DATA: COMMERCE DEPT., BW

changed during the past five months. Board officials say that it shows only faint signs that a recovery is even in progress and no signs of a vigorous rebound.

It's becoming increasingly likely that consumers went on a onetime spending spree last quarter, satisfying some of the demand that had built up during the Persian Gulf war. Weak fundamental supports, combined with the failure of confidence to extend its postwar rally, suggest that consumers may not have much more to contribute to the recovery. A new round of retrenchment by consumers is a sure formula for a double dip.



The big offset to strong consumer demand last quarter was a sharp deterioration in the trade balance. Trade swung from a \$7.1 billion surplus in the first quarter to an \$18.6 billion deficit, adjusted for import and export prices. Exports grew by \$5.9 billion, but imports surged by \$31.6 billion.

Import-led improvement in the trade balance was the single biggest cushion under the economy during the recession. Weak demand by consumers and businesses produced the largest two-quarter drop in imports in a decade.

Now, those import declines are over, and exports are slowing in response to weaker economies abroad and a costlier dollar. During the first half, exports grew at an annual rate of 2.1%, down from their 5.8% pace in 1990.

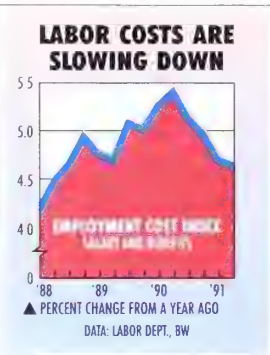
BUILDERS FACE A MIXED OUTLOOK

Except for homebuilders, any big contribution to demand from the business sector is a long way off. Businesses will not lay out money for new construction or equipment until they see a solid recovery taking hold.

Construction is shaping up to be a mixed bag in the second half, with little net contribution to GNP. Residen-

tial contractors have been encouraged by the bounce in home sales and are lifting their investment in new projects. But the outlook for nonresidential construction, such as commercial and office building, remains bleak.

Residential construction rose at an annual rate of 2.1% last quarter, the first gain in a year, as sales of single-family homes continued to rise. In June, sales jumped 7.4%, to an annual rate of 525,000. Sales are up 27% from their January low point (chart). However, residential construction fell further last quarter, down to a 4.5% annual rate, and the slide isn't over yet.



New contracts, a leading indicator of construction spending, show the split in the outlook. Contracts dropped 4% in July, as residential building rose 2% but the nonresidential sector posted a 6% drop to the lowest level since the 1981-82 recession, says the F. W. Dodge Group, division of McGraw-Hill Inc.

Business outlays for equipment face an uphill battle

as well. The GNP report showed that equipment spending fell at an annual rate of 1.6% last quarter. Because capital spending lags behind the overall business cycle, and since new orders for capital goods are still falling, equipment outlays may not turn around before year's end.

About the best thing that can be said about a weak recovery is the prospect it provides for lower inflation. In addition to tamer-looking price indexes in recent months, labor costs continue to moderate (chart). During the past year, compensation costs, including wages and benefits, rose 4.6%, down from 5.4% in the previous year.

Since labor accounts for the lion's share of business costs, that slowdown bodes well for further decline in inflation. Of course, if the double-dippers turn out to be right, inflation improvement would be stunning.

THE WEEK AHEAD

CAR SALES

Monday, Aug. 5, 5 p.m.

Sales of domestically made cars in the final 10-day period of July are expected to come in at an annual rate of 6.8 million, according to a survey of economists by McGraw-Hill's MMS International. That would lift July sales to a 6.9 million pace from 6.7 million in June and from 6.1 million in May. However, some of the recent strength may be temporary. Large fleet purchases by rental-car companies have boosted sales.

PRODUCTIVITY

Tuesday, Aug. 6, 8:30 a.m.

Productivity, measured as output per hour in the nonfarm economy, probably

rose at an annual rate of about 2% in the second quarter. The economy's gross domestic product rose a little more than 1% last quarter, while hours worked fell 1%. Productivity has not posted a gain of that size in nearly three years. It typically rebounds during a recovery, as companies boost output by working existing employees longer hours, before they add workers back to their payrolls.

INSTALLMENT CREDIT

Wednesday, Aug. 7

The MMS economists expect consumer installment credit for June to show a slim gain of \$500 million. This net of new extensions over repayments has slowed sharply in recent months, as consumers try to lighten their debt burdens. Install-

ment credit dropped by \$626 million in May, and since last October it has fallen by an average of \$320 million per month.

PRODUCER PRICE INDEX

Friday, Aug. 9, 8:30 a.m.

The producer price index for finished goods for July is expected to show a slim 0.1% gain, according to the economists in the MMS survey. Energy prices fell slightly, and food prices were unchanged. The PPI fell 0.3% in June. Excluding the volatile food and energy sectors, the core PPI is expected to rise a modest 0.2%. If the projections are on target, the core rate of inflation in producer prices, measured from a year ago, will slip to the slowest pace in about three years.

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AND THE CRUNCH GOES ON

BORROWING WILL JUST GET TOUGHER—UNLESS YOU'RE A MEGACORPORATION

Call it the case of the chronic credit crunch. Early in the recession, bad-loan-blighted banks were scared into lending warily. Now that the recession is ending, another type of big-league lender has joined them: insurers. They're spooked by several collapses, most recently that of Mutual Benefit Life Insurance Co.

This is bad news for smaller companies and highly leveraged outfits, which will remain *personae non gratae* to lenders. But big public companies will benefit from investors' flight to quality, even though one manifestation will be heavy purchases of U.S. Treasury securities. For big companies, the recession's end will make capital even easier to come by. There will be "a good availability of funds for investment-grade markets. But things will be tight for everyone else," says David W. Mullins Jr., vice-chairman at the Federal Reserve. Adds Frank V. Cahouet, chairman of Mellon Bank Corp.: "A whole segment of companies won't get financing and will atrophy. You'll have to wait four years for this to loosen up."

Just ask U.S. Home Corp., a Houston homebuilder whose erratic fortunes after the early-'80s oil bust made lenders leery. This year, U.S. Home needed more money from its 17 bank lenders to complete several partially built projects, put their houses on the market, and generate some much-needed revenue. No dice. Lenders "were nervous about real estate," says spokeswoman Kelly So-moza. Result: The company last April tumbled into Chapter 11 bankruptcy.

BIG HANGOVER. Worse yet, smaller businesses are being cut out of the credit flow. They are a key source of innovation, and, by some calculations, create more than half of all new jobs. Yet borrowing by small businesses has weakened more sharply than in previous recessions. Their outstanding debt has declined during the past two quarters—the first time that has happened in the 40 years such data have been tracked,

according to Kidder, Peabody & Co. In many cases, says economist David L. Birch, president of consultant Cognetics Inc., "the bank will just call up and cancel all their lines of credit."

More broadly, some economists fear that the credit crunch is partly to blame for the nation's current slow money-supply growth, which may threaten the recovery unless the Federal Reserve takes

action by lowering interest rates. The sluggish money supply mostly fleets money moving out of the bank system, while other indicators of economic activity, such as housing, point to recovery. Nonetheless, something we're watching closely," says Fed Governor Edward W. Kelley.

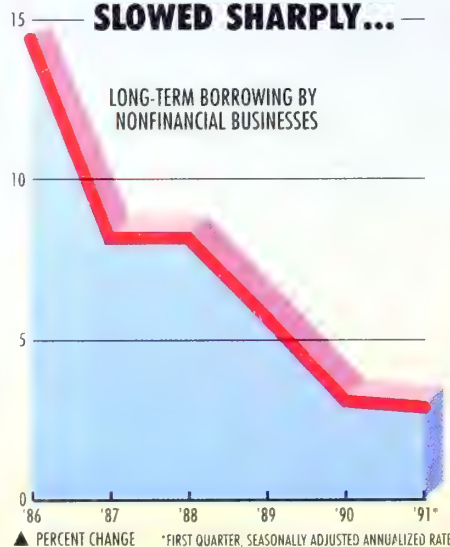
What's holding back banks, insurers and other lenders is the hangover from

THE NEW DIMENSIONS OF THE CREDIT CRUNCH



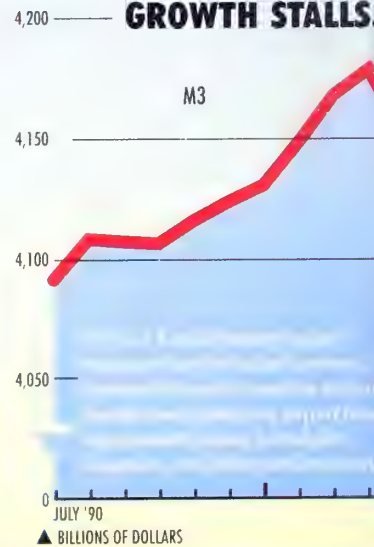
■ MUTUAL BENEFIT LIFE'S FALL HAS INSURERS SPOOKED

BORROWING HAS SLOWED SHARPLY...



DATA: SMITH BARNEY, HARRIS UPHAM & CO

...AS MONEY GROWTH STALLS.



DATA: FEDERAL RESERVE

dered past investments, especially commercial real estate. The office vacancy rate in 1991's first quarter was 10% in the cities and 22% in the suburbs, according to Salomon Brothers Inc. About it: That's the equivalent of five office buildings standing idle. Mutual Benefit's demise was due to its heavy mortgage defaults—10% at the end of 1990.

burned, twice shy. So banks and insurers are avoiding other areas they deem too risky. Aetna Life & Casualty is steering clear of junk bonds and is being very picky about private placements that are often sustenance for mortgage companies (charts).

TIER. Of course, the Exxons, and Philip Morris of this world have had trouble collaring capital. In this pantheon, the new golden rule is almost any publicly traded company with a strong balance sheet or business prospects. Even highly levered companies are welcome if their cash flow is sound enough: Duracell,

Safeway Stores, and Caldor had no problem floating recent stock offerings. Edward E. Yardeni, chief economist at C. J. Lawrence Inc., says that unlike the 1980s, when the stock market often concentrated on financing buyouts, it now is an arena for raising capital to grow.

Lenders are willing to take another

'A whole segment of companies won't get financing and will atrophy'

pass at companies able to demonstrate equity investors' confidence, although doing so can be hard work. Energy Ventures Inc., a small oil-field service company in Houston, approached a group of insurers for a private placement loan of about \$40 million. The insurers were squeamish, even though the company can easily cover its current debt of \$37

million. But after a strong 1990, Energy Venture's earnings had slumped a bit. So the company raised money first by a \$17.5 million stock offering on July 10. Now, it has a sporting chance of tapping the insurers, says P. Blake Dupuis, the company's chief financial officer.

Stock offerings have been selling at full tilt. Initial public offerings are up 35% over the comparable stretch last year—injecting billions into fledgling companies. The IPO boom, though, hasn't helped in such out-of-favor areas as chemicals, steel, and publishing.

Other financial trends are good news to top U.S. corporations. Commercial bank lending may be down, but the gap has been partly filled by other lenders, such as the commercial paper market. Also helping the big boys are lower short-term interest rates. Since about 50% of all corporate debt is short-term, the corporate interest bill will drop over the next year. Indeed, interest rates declined even after the Treasury announced on July 31 that it will borrow some \$190 billion over the next five months. Rates dropped because the size of the planned borrowings was no surprise. Blue-chip borrowers should also benefit as investors seeking higher returns flock to bond and stock funds, which prefer big-company investments.

ROUGH JUSTICE? This could be the start of a trend. Equities have long been a declining share of household financial assets—dropping from 35% in the late 1960s to less than 20% currently. "But there will be a significant restructuring of individual investor portfolios away from residential real estate and other real assets and into financial assets in the 1990s," says Steven G. Einhorn, a partner at Goldman, Sachs & Co.

Foreign capital is another source of strength for big corporations. In 1990, foreign investors acquired a net \$5.9 billion in American corporate bonds and slashed stock holdings by \$16 billion. But annualizing 1991's first quarter shows them buying \$24.3 billion in bonds and \$10.9 billion in stock.

In Darwinian terms, continued tight credit for the less creditworthy may mete out a certain rough justice for the last decade's highfliers. But some deserving little companies or larger highly leveraged enterprises, trying to ride out a sluggish economy, figure to get starved in the process. And that could well deprive business of a good share of the innovation and competition that keeps the economy vibrant.

By Larry Light and Christopher Farrell in New York, with Mike McNamee in Washington, Lisa Driscoll in New Haven, and Mark Ivey in Houston

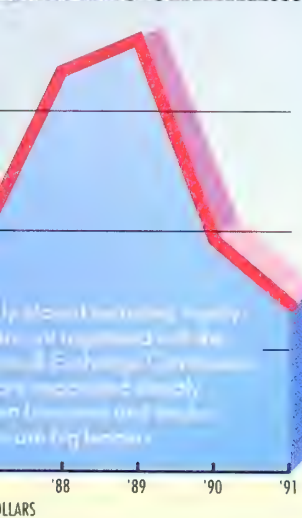


PROJECTS WERE STALLED

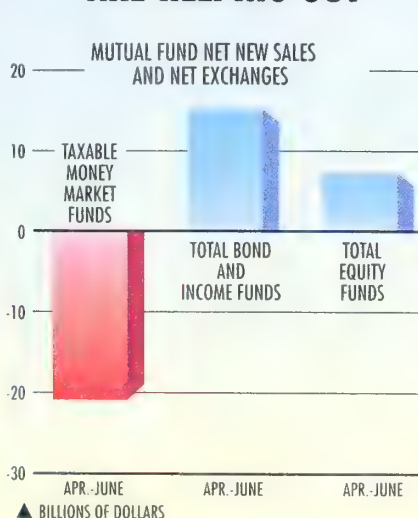


■ LINING UP TO BUY TREASURIES IN CHICAGO

...AND PRIVATE PLACEMENTS SHRINK...



...BUT SMALL INVESTORS ARE HELPING OUT



DIPLOMACY



BUSH AT CEREMONIES DURING THE MOSCOW SUMMIT: AN ARMS-CONTROL TRIUMPH

EYEBALL TO EYEBALL IN MOSCOW —OVER REFORM

Bush and Gorbachev disagree on who should make the next moves

The symbolism in the Kremlin's grandest hall was tailor-made for George Bush. At the ceremonies that marked the beginning and ending of his first Moscow summit with Soviet leader Mikhail Gorbachev, Bush stood before a huge bas-relief depicting the legend of St. George slaying the dragon. In signing the first-ever agreement to reduce long-range nuclear arsenals, the President could take half the credit for taming the cold war's most terrifying demon. But in trying to move ahead into a new era of cooperative U.S.-Soviet relations, the President got a firsthand glimpse in Moscow of just how elusive his new prey is likely to be.

Even as the leaders signed the START treaty on July 31, economic links and internal Soviet politics succeeded arms control as the focal point of U.S.-Soviet discussion. And those new concerns brought disquiet to a successful and tightly managed summit. For much as Washington and Moscow both entered the START negotiations 10

years ago willing to succeed but unwilling to take the first bold steps to achieve success, so they each wait for the other to make the first move in the long and perilous process of fully integrating the Soviet Union into the global economy.

The leaders capped their arms-control triumph by announcing plans to issue invitations to an October conference on Arab-Israeli peace, and Bush dispatched Secretary of State James A. Baker III to Jerusalem to secure the final details of Israel's participation. But just hours af-

ter Bush unveiled a string of economic initiatives, in particular granting Moscow most-favored-nation trading status, Gorbachev was back pressing for more. There is "an increasingly obvious discrepancy between the range and scope of our political dialogue, including arms control, and the nature of our economic relations," the Soviet leader chided.

STILL TIPTOEING. Gorbachev is convinced that to take such jarring reform measures as forcing the quick convertibility of the ruble, he must have precisely the kind of help from Washington that poses the greatest political risk to the cautious U.S. President. In Moscow, Gorbachev stressed steps already backed by Washington's European allies, such as dismantling Western aid and scrapping export controls that Gorbachev blames for holding up billions of dollars of pending investment projects. But Washington remains unconvinced that such steps will help the Soviet Union that has so far only tiptoed into reform. "Gorbachev's argument that these reforms are as much in his interest as in mine, and that's not my view," says one senior Administration official.

As Moscow moves down the reform road, such frictions will only grow. One of the hottest spots right now is conflict over the conversion of Soviet defense plants to civilian production, seen as critical to economic reform. Bush's approach is to start small, through steps such as having Soviet defense plant managers visit U.S. defense contractors. But even reform-minded Soviet industrialists believe that without direct Western investment and a loosening of export controls to permit technological renovation, the process will flounder. After World War II, "the U.S. helped Japan convert, and West Germany had the Marshall Plan, but now the U.S. is on the brakes," complains Vladimir I. Volsky, head of Moscow's most powerful business lobby (page 23).

For Bush, navigating the sandbars of Soviet internal politics may prove even trickier than fending off Soviet calls for more money. In Moscow, the President put his close relationship with Gorbachev at some risk by venturing out to meet with Russian Republic President Boris Yeltsin and officials of other republics. And in the independence-minded Ukraine, which is contemplating establishing its own currency, Bush on Aug. 1 stressed the premise that foreign invest-

BONES OF CONTENTION

Bush and Gorbachev are far apart on the means to many ends

DEFENSE CONVERSION

- ▶ Bush favors a go-slow policy, consisting mainly of technical advice to Soviet managers
- ▶ Gorbachev wants direct aid and loosening of controls on exports to the Soviet Union

ECONOMIC REFORM

- ▶ Gorbachev has little interest in an International Monetary Fund reform plan that doesn't have dollar signs attached to it
- ▶ Bush fears that loans without reforms would be a waste of money

CLIENT STATES

- ▶ The Administration argues that cutting Castro loose would show good faith
- ▶ Need for Communist Party support compels Gorbachev to maintain his ties to the Cuban dictator

DATA: BW

pace on a unified Soviet market. Ukrainians have their own agenda, and aren't likely to be swayed by Western advice, whatever the source. **FIDEL.** Gorbachev isn't likely to respond to Bush's call to turn his back on the dictator Fidel Castro. The Soviet Union still needs to placate Communist stalwarts and has little choice but to maintain warm relations with Cuba. Washington and Bush may also find a hinting lack of stability flowing from the all-union treaty that Gorbachev will soon be signed. A major stumbling block: a continued fight be-

tween Moscow and the Ukraine over whether the center or the individual republics control the right to tax. And Bush's new political contacts may in the end be of limited use. "Most of the people Bush was to see in Moscow won't be around in a year, at least not politically," says Dmitri K. Simes, a Soviet specialist at the Carnegie Endowment for International Peace.

Such shifting political sands won't offer Bush much of a foundation to build the new era he seeks. And with Soviet gross national product falling at an annual rate of at least 10% in the first half

of this year, Gorbachev's worsening economic and political woes will make it tougher and more urgent for him to undertake painful reforms. Over time, that may leave the Bush-Gorbachev Moscow summit remembered for the reversal it brought to the superpower agenda. While arms control seems destined to become an exercise in technical details, economic and political links between the superpowers could easily take on the trappings of brinkmanship that once marked the arms race.

By Bill Javetski and Rose Brady in Moscow

FROM APPARATCHIK TO 'MR. BUSINESS' IN MOSCOW

When IBM wanted to set up the first 100% Western-owned subsidiary in the Soviet Union, a former Communist Party apparatchik named Arkady I. Volsky successfully piloted the deal through Moscow's notorious bureaucracy. Top executives, including General Electric CEO John F. Welch Jr. and Grace Chairman J. Peter Grace, early troop through Volsky's eleventh office, testing the investment waters. And when President Bush headed for Moscow, his top economic aides met out trade and investment issues for two hours with the Marlboroughing Volsky.

Who is Arkady Volsky? Although his name is almost unknown outside a small circle of Western executives and Kremlinologists, the 59-year-old Volsky is becoming a crucial figure in the Soviet Union's switch to a market economy. The League of Scientific & Industrial Associations of the U. S. S. R., the leading group he heads, represents 65% of Soviet industrial output. It resembles a National Association of Manufacturers with an open-door policy and members range from restaurants and computer startups to state-owned industrial giants.

His friend and ally Gorbachev shares the risks of plunging headlong into the most painful reforms, Volsky's job is to line up business support to make or break *perestroika*. It also determines the ambitious leader's own political future.

GROUND. Volsky's aim is to establish a business climate that Western investors can rely on, that isn't at the mercy of every shift in momentum in the tug-of-war between Moscow and the republics. With enterprises from all Soviet republics taking part in the industrial league, Volsky is helping set up a network of commercial banks, insurance companies, and schools of en-

trepreneurship to stimulate trade among the republics, and by extension, with the West. "Everybody is talking about the market, but no one else is setting it up," says the poker-faced, graying Volsky. Perhaps most important, he adds, the league is working behind the scenes with enterprises and government officials to craft an economic agreement guaranteeing a sin-



VOLSKY: "EVERYBODY IS TALKING ABOUT THE MARKET, BUT NO ONE ELSE IS SETTING IT UP"

gle currency and uniform customs rules throughout the Soviet Union.

Moscow's "Mr. Business" has undergone a personal transformation no less dramatic and difficult than his country's. Volsky started out as a textbook Soviet industrial manager. Trained as a steel engineer, he worked his way from foreman's assistant to chief of the foundry division at the sprawling Zil

auto and truck factory in Moscow. In the early 1970s, he became the Communist Party boss in charge of developing the country's engineering industry, handing down orders to build the giant Kamaz truck factory in central Russia and the Volga auto works in Togliatti.

As an aide to Soviet leader Yuri Andropov in the early 1980s, Volsky got a brief, heady taste of economic reform. By the time Gorbachev, a longtime associate, started his reforms in 1988, Volsky was ready to abandon his career as party apparatchik and reestablish the industrial league, which had flourished before the 1917 revolution.

REBUILDING BRAINS. If Volsky's current venture is to succeed, his biggest challenge may be convincing a whole generation of command-economy advocates to follow his path. "For 73 years our ideology has been hammering into the heads of Soviet citizens, that private property is bad, that the market is an inferno," Volsky says. "It is very difficult for people to rebuild their brains."

Gorbachev's own future could ride on Volsky's ability to win over the factory directors and generals who hold the swing votes between reformers and reactionaries. The job would test the most persuasive salesman: As entire towns devoted to defense production wither, some military factory directors "think the drop in living standards is due to the market," Volsky worries. "But that's not so."

Market reforms may now depend more on Volsky, with his links to factory managers, than on Gorbachev. Pulling off such a job could well vault Volsky into the Prime Minister's office that Moscow politicians say he covets. Western CEOs—and the embattled Soviet leader himself—are waiting to see if Volsky can deliver the goods.

By Rose Brady and Bill Javetski in Moscow

Arkady Volsky's industrial league aims to establish a business climate Western investors can rely on

Commentary/by Susan B. Garland

MAKING UNEMPLOYMENT FUNDS WORK OVERTIME

Few bills kicking around Capitol Hill have as much political allure as measures that extend unemployment insurance to the hapless recession victims who have exhausted their benefits. On July 30, Democrats pushed through legislation in the House Ways & Means Committee that would stretch benefits beyond the current 26 weeks. Despite worries about the costs, even some Republicans favor the bill, which is moving quickly through both houses. The extra money undoubtedly will help thousands of the unemployed put food on the table. But unaddressed is an even bigger problem: helping the jobless adjust to a rapidly changing economy.

That wasn't a concern in 1935, when Congress created the unemployment insurance program. The system was designed to provide temporary income for laid-off workers during short downturns. These days, though, structural changes in the economy mean that many employees will never return to their old jobs, particularly those in declining Rust Belt industries. Labor Dept. data show that the number of workers who were jobless after 26 weeks rose to 921,000 in February, compared with 659,000 in June, 1990—a 40% boost. Many will have to upgrade their skills, and some will have to change occupations.

NOW HIRING. The venerable unemployment system does nothing to prepare the jobless for new work. Indeed, it bars the use of federal unemployment insurance benefits for job searches, training, and other measures to help workers move into new fields. Instead of simply handing out more money to the jobless, as the pending legislation proposes, Congress should redirect the program to deal with job-market realities. Some Labor Dept. experiments suggest that's a real possibility.

Ask James A. O'Neill Jr., 45, of Westfield, Mass., a manufacturing manager who was laid off last August

from National Metal Industries. Thanks to the Enterprise Project, operated by the Massachusetts Employment & Training Dept., O'Neill now runs a consulting firm, CompControl Inc., which advises employers on reducing workers' compensation costs. Business is so brisk that O'Neill has already hired two part-time workers.

O'Neill's experience shows how a lit-

benefits than the average unemployed insurance recipient. The budget-battered state is pleased, and so is O'Neill. "I don't think I would have this business otherwise," he says.

Of course, entrepreneurship isn't for everyone. But an earlier demonstration project, in New Jersey, holds out hope for other dislocated workers. From July, 1986, to June, 1987, nearly 9.0

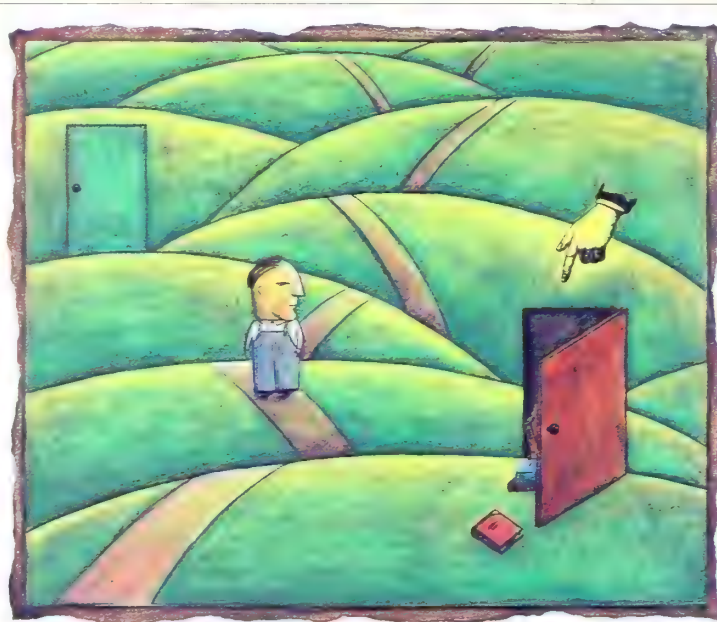
unemployed took advantage of such services: bonuses for rejoining the work force early, short-term training, and job-search workshops. Participants tended to find jobs sooner than the average unemployed insurance recipient and at a somewhat higher wage than they were earning before they went on unemployment.

'ONLY OPTION.' The program was most successful with those who have marketable skills, such as clerical and white-collar workers. "For the group that has obsolete skills, training is the only option," says Walter Corson, vice-president of Mathematica

Policy Research Inc., the project consultant. "But it is expensive and takes a long time to do."

Right now, states can't use federal unemployment funds for such unconventional services. The federal Job Training Partnership Act of 1982 covers a small percentage of dislocated workers. States may use their own money to provide intensive job-search support, and some do. But startup costs are high, and the recession makes it hard to offer such assistance.

The pending legislation includes money for more demonstration projects but leaves the basic scheme intact. Undoubtedly the effort is swell politics and it gives the Democrats a great issue with which to cudgel "heartless" Republicans. But the partisan roar is drowning out a key fact: Extended benefits will help workers survive layoffs. Fundamental reform could sharply reduce the number of workers who need benefits in the first place.



tle creativity can invigorate the unemployment system. To launch the initiative, Massachusetts needed a waiver from a federal law that requires all unemployment insurance recipients to be looking for work. The three-year project, which began last year, suspends that rule and pays standard weekly benefits to budding entrepreneurs. It also provides them with new-business workshops. A project in Washington state pays recently laid-off workers a portion of their benefits in a lump sum as new-business seed money.

Participants in the Massachusetts project's first year collected 13% less in

Massachusetts and Washington State are successfully using benefits to encourage entrepreneurs

HERE ARE TROUBLED BANKS, AND THEN THERE'S FIRST AMERICAN

Ownership is only one of its woes—legal and otherwise

It has been the talk of the town ever since a Bank of Credit & Commerce International executive bragged to federal agents in 1988 that Luxembourg-based rogue bank had secretly owned Washington's First American Bankshares Inc. for the past years. Despite that, it took the Fed to reserve until March to order BCCI First American. But now, with criticism by British regulators and information for money laundering and fraud in New York, U.S. investigators are finally turning up the heat on top officials of the \$11 billion bank group.

The Fed, the Justice Dept., two congressional panels, and the Manhattan District Attorney's office all want to know whether First American's chairman, Washington superlawyer Clark M. Clifford, and president, Robert A. Altman, lied when they assured the Fed that the bank was independent of BCCI. Both their lawyer, both deny any wrongdoing. But the Fed maintains that the founder Agha Hasan Abedi and officials recruited senior BCCI executives for First American's New York office, even paying them extra salaries.

MONEY. Despite such disclosures, investigators have yet to find any sign that First American took part in the money laundering schemes that government officials say pervaded BCCI. The bank didn't even collect any dividends, sources say, although First American's assets and profits grew at a 20%-a-year clip through the 1980s. There is still evidence that First American was funneling any funds for BCCI," says a Fed official. Whatever strategy the bank had for its U.S. affiliate, it's now unraveling.

On July 29, the Fed fined BCCI \$200 million for illegally acquiring the bank. The charges that BCCI gained control of First American in 1982 by lending to Middle Eastern front men. With ownership of the bank thus clouded, the bank's sale to BCCI's stake have ground to a halt. What's more, the bad publicity surrounding BCCI is beginning to take a toll on First American: Since June, 1990, the bank has lost some \$500 million in deposits.

Big depositors say they fear that First American gets into trouble, the government won't protect accounts over the \$100,000 federal insurance limit. For example, even before the Bank of

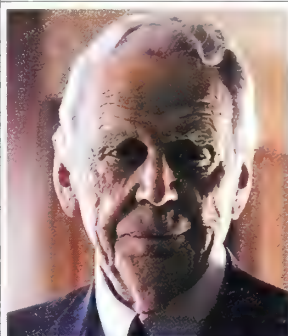
England seized BCCI on July 5, Tom Condit, president of Washington's National Cooperative Bank, pulled several short-term deposits worth more than \$1.5 million. So far, smaller savers haven't followed suit.

First American is suffering, though. Washington's real estate woes forced a \$158 million loss in 1990, and this year looks no better. Nonperforming loans at First American's five banks tripled, to \$469.8 million, between March, 1990, and

Saudi Arabia. BCCI's front men pledged part of their stake in First American's parent to secure \$390 million in loans and repurchase agreements from Mahfouz. They then paid off their loans from BCCI, bolstering its balance sheet.

Once BCCI was past its funding crisis, the Fed says, it bought back the stock from Mahfouz, lending the funds to the same front men to make the purchase. The loans inflated BCCI's assets, even though the transaction was a sham. Says a U.S. investigator: "They were moving the shares around in circles, and the loans just kept getting bigger and bigger." As part of the deal, BCCI lent Clifford and Altman money to buy shares in the parent firm. They later sold some of them at a \$14.2 million profit.

Whether BCCI had an even deeper involvement with First American is yet to



FIRST AMERICAN'S CLARK CLIFFORD (TOP) AND ROBERT ALTMAN: WERE THEY REALLY IGNORANT ABOUT TIES TO BCCI?



March, 1991. On Apr. 18, First American's Washington bank signed an agreement with regulators to work out bad loans, improve appraisals, and boost its capital. First American also set aside \$230 million in reserves.

Investigators have found only one clear way in which BCCI exploited its ownership of First American. The Fed maintains that BCCI, which suffered a huge trading loss in 1986, pumped up its balance sheet by manipulating the shares of First American's parent firm.

To raise funds, says the Fed, BCCI turned to Khalid bin Salim bin Mahfouz, owner of National Commercial Bank of

be determined. First American's New York bank, for example, served for years as one of several U.S. clearing agents for the Luxembourg bank. That relationship and others may come under increased scrutiny in coming weeks. In announcing the indictments of BCCI and its founder on July 29, Manhattan District Attorney Robert M. Morgenthau said that only "20% to 25% of what ultimately will be the result of the investigation" has emerged so far. It's unlikely the other 75% will do anything to ease First American's woes.

By Catherine Yang and Mike McNamee, with Tim Smart, in Washington



POLKAS AND MAZURKAS: THE CROSS-CULTURAL TRAINING PROGRAM INCLUDES FOLK DANCING

FROM THE HALLS OF U.S. B-SCHOOLS TO THE MILLS OF HUNGARY

The fledgling MBA Enterprise Corps sends managers to Eastern Europe

In the 1960s, thousands of young Americans answered John F. Kennedy's call to serve their country by joining the newly formed Peace Corps. But idealism was hard to find in the 1980s, when many of America's best and brightest viewed a degree in business, law, or medicine as a ticket to riches.

But wait. Consider Jeffrey Rosen, Columbia business school, 1991. Although he's burdened by \$20,000 in school loans, Rosen just turned down a \$50,000-a-year offer from American Telephone & Telegraph Co. Instead, he's off to Czechoslovakia, where he'll earn \$150 a month as a manager at Prague Energy Works, a state-owned utility in the throes of privatization. "There's a lot more to a job than the salary," Rosen says. "I want to participate in change."

NO DITCHDIGGERS. Rosen, 24, isn't alone. He belongs to the fledgling MBA Enterprise Corps, a sort of Peace Corps for the finance-and-marketing set. The group was formed last year by a 16-school consortium headed by the University of North Carolina's Kenan-Flagler Business School (table). In August, the corps will send the 41 members of its first class to Czechoslovakia, Poland, and Hungary, where they'll spend at least a year working for government agencies and newly privatized business-

es. The MBAs will draw up business plans, locate financing, and develop export operations.

What's in it for them? The pay and lodging are modest at best, but the overseas experience is invaluable. "Getting into international business is very difficult for Americans without firsthand foreign experience," says Margaret Minichini, a 1991 grad of Kenan-Flagler. Before earning her MBA, Minichini worked for Federal Express Corp. This fall, she'll help Postbank of Czechoslovakia set up financial-service centers in post offices. Says Michael Peprnik, a Postbank personnel director: "We hope she can give us a lot of help."

The inspiration for the MBA Enterprise Corps came from a speech given by entrepreneur H. Ross Perot at Chapel Hill, N.C., two years ago, in which he challenged students to lend a hand in Eastern Eu-

rope. "It popped into my head that should form a corps," says Jack Behrman, a retired UNC professor and director of the MBA Enterprise Corp.

During a May, 1990, trip to Poland, Czechoslovakia, Hungary, and Yugoslavia, Behrman and a group of UNC professors met with nearly 100 government officials, academics, and consultants. "Everybody was enthusiastic until I mentioned the word 'students,'" says Behrman. But after Behrman explained that most graduates of top B-schools have several years of work experience, the idea of an MBA corps caught on.

'BOOT CAMP.' UNC was one of dozens of American B-schools checking out Eastern Europe. To keep confusion to a minimum, a consortium was formed that included nearly all the top U.S. schools—except Harvard University and Massachusetts Institute of Technology, both of which declined to join. Funded by the Agency for International Development (AID) and UNC's Kenan Institute of Private Enterprise, the nonprofit consortium gives each MBA a stipend of \$300 a month and sets aside \$330 a month more to be collected upon returning home.

To prepare for assignments overseas, the MBAs have spent the past three weeks in Chapel Hill, devoting 10 hours a day, six days a week, to language and cross-cultural training, including folk dancing. After the MBAs arrive overseas, they'll get a further three weeks of instruction from the program's co-sponsors in Eastern Europe. Since there are no real business schools in Hungary, Poland, or Czechoslovakia, the MBA consortium has recruited groups such as Prague's Center for Democracy & Enterprise to be co-sponsors.

The MBAs don't see themselves as

shock troops of American capitalism. Says George Phipps, a Stanford University MBA who'll be working with the U.S.-backed Czech and Slovak American Enterprise Fund: "I'm like a therapist. I can't tell them what they need, but hopefully I can help them discover it for themselves." These MBAs may not be as idealistic as the first Peace Corps recruits, but all the same, they could end up changing the world.

By Monica Roman
New York, with
Reichlin in Bonn

THE CORPS AT A GLANCE

LOCATION

UNC, Chapel Hill

PARTICIPATING SCHOOLS

16, including Cornell, Northwestern, and Duke

NUMBER OF STUDENTS

41 MBAs

LENGTH OF TRAINING

Six weeks

CURRICULUM

Language courses, history, cultural studies

LENGTH OF FOREIGN TOUR

12 months, renewable

DATA: MBA ENTERPRISE CORPS

E 'BLACKTOP' IS PAVING REEBOK'S ROAD TO RECOVERY

Designed shoe for city youth should sell 2.2 million pairs this year

...thing we do, I want to do a little different. That's what it's all about.

—John H. Duerden, senior vice-president, Reebok International Ltd.

...one tries to beat someone with something different. That's the way it should be.

—Archie Megel, 12
Dorchester, Mass.

John H. Duerden sells a basketball shoe for the Blacktop that Archie Megel like to be wearing right now. The Blacktop is, in fact, this summer's mass-market expression of individual difference on America's city streets. By far. Months into its commercial life, it has sold out of many stores. By year-end, Reebok expects to have delivered to retailers some 2.2 million pairs.

Why the fuss over a \$69 sneaker? Reebok says it's because the Blacktop, which has a tough sole and heavy leathers, is built especially for punishment on urban outdoor courts. But everyone is buying this argument. "It's kind of silly," says a spokesman for Nike Inc., which, like Converse Inc.,

plans to produce a similar shoe. But Reebok's biological marvel, the Blacktop, is a singular success. It shows that Reebok has learned something new about the market—and thus is catching up to Nike, which stole the athletic footwear market two years ago. Reebok's must-have shoe has helped it gain three years of

lost U.S. sales and falling market share. In this year's weak market, Reebok's revenues are up 10% so far. Nike's sales dropped 6% in its latest quarter. Those two numbers alone tell you who's going on," says analyst Gary M. Johnson at Kidder Peabody & Co.

ED UP. Indeed, Reebok finally is giving itself something more than a tagline: aerobics-shoe maker. Boosted by \$10 million from the Blacktop, an additional \$250 million from inflatable Pump shoes, and enormous international

growth, total revenues should climb 27% this year, to \$2.75 billion. Even Reebok's long-suffering Boston Whaler Inc. boat division is turning up. That's why Reebok shares have more than doubled since Dec. 31, to 28.

The Blacktop shows how Reebok has improved its game. While touring with a company program called "Court Renewal," which has rebuilt 26 outdoor playgrounds across the country, executives met city players and "kept hearing

hit upon the notion of selling a shoe specifically for outdoor city play. "It's a concept that's been staring everyone in the face for years, and no one's done anything," says Larry Bresnick, a buyer for the Foot Locker retail chain. Nike and Converse say their shoes play well indoors or out. L. A. Gear Inc. is working on a street shoe for next spring.

REGULAR GUYS. Reebok backed its idea by sponsoring a nationwide three-on-three basketball tournament—a grassroots effort that has helped defuse criticism from groups such as Operation PUSH that athletic-shoe makers exploit black youths. Then, there's a \$6.5 million advertising splash. But rather than spotlighting a pro-ball demigod, the campaign stars Sinbad, a popular black comedian. "How do you know when you're out of bounds?" Sinbad asks in one spot. "When you hit the trash can, you've



COURTING FAVOR: 80% OF CONSUMERS BUY SNEAKERS JUST FOR LOOKS

REEBOK'S COMING BACK



about how fast shoes wear out," says Senior Marketing Director John Morgan.

Reebok's answer: a sneaker that's two to three ounces heavier than its competitors',

moderately priced, and promoted for its performance on asphalt and concrete. Does the race-car-tire-rubber compound really make a difference? Maybe, maybe not, say players. As it happens, the Blacktop looks good, so it appeals to the 80% of consumers who buy athletic shoes solely for fashion. But performance matters, too. Ask Tony Harris, a Dorchester player. "You can get any black-and-white sneaker," he says. "It doesn't matter how it looks."

More important, no one else had ever

gone too far." The message: Regular guys play outdoor ball.

That street-level image will be at the heart of the new corporate ad campaign Reebok will unveil on Aug. 5. "Performance with a human face," is how Duerden, who heads the company's footwear division, describes it. Reebok won't reveal much about the new ads except their tagline, reminiscent of Nike's now-ubiquitous "Just do it." Reebok's answer: "Life is short. Play hard."

More than a slogan? Well, Reebok sells image, not shoes. To that extent, the company is as vulnerable to whim as any other apparel outfit. But as Blacktops are proving, Reebok has the smarts to come up with the slam-dunk image the market is looking for.

By Keith H. Hammonds in Stoughton, Mass.

Déjà Vu

THE NEW COMPAQ DESKPRO 486/50L.

Seems we've been here before. Once again, the most powerful PC you can buy—in fact, the most powerful in existence—comes from Compaq.

The new COMPAQ DESKPRO 486/50L Personal Computer has everything for the most voracious power users, and for intensely

demanding networks. It has Intel's fastest, most powerful microprocessor—the 50-MHz 486 (more than 50% faster than the 33-MHz 486). A second-level cache so big (256 Kbytes) that 99% of the time, the data you need will be instantly accessible. A more-than-generous 8 megabytes standard RAM. Plus dozens of

other features for speed and top performance.

Every component is carefully chosen, tested and perfected to make sure they work together to deliver the maximum performance possible.

Who's it for? Designers and engineers longing to stretch CAD/CAE to its limits. Software developers who want compilation without limitation. Scientists who seek

boom.



erated analysis. Anyone who wants
h Windows wide open and watch
ics-based applications fly.
What's good for one power user is also
or a group. Exceptional speed, expand-
and practically limitless storage (more
0 GB) make it an extraordinary network
and multiuser host.
but doing something this new and

exciting isn't new to us. Compaq has a
history of building the top-performing PCs
in their class. With the highest standards
of reliability (to save you money) and
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And outstanding support.

The Compaq Customer Support
Center at 1-800-345-1518 puts you in touch
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complement your dealer's know-how.

For details and the location of your
nearest Authorized COMPAQ Computer
Dealer, call 1-800-231-0900, Operator 164.
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COMPAQ

It simply works better.

SAKS FIFTH AVENUE HAS SEVENTH AVENUE SHAKING

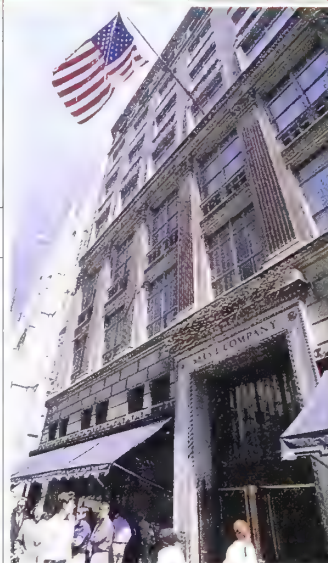
The chain refuses to reveal financial data

The rumor has been circulating for months: Saks Fifth Avenue is in trouble. Many suppliers and creditors say they haven't gotten any word about the elegant department-store chain's operating results since August, 1990. In July, two apparel credit reporting agencies, Bernard Sands Credit Consultants and Credit Exchange Inc., said that they had stopped recommending Saks to their clients. Then, Heller Financial Inc., a large factoring company, stopped approving shipments of merchandise to Saks. Now, many on Seventh Avenue worry that Saks may be hiding something.

In early June, Saks Chairman Melvin Jacobs assured *BUSINESS WEEK* that business was good. But since then, *Women's Wear Daily* asserted that Saks lost as much as \$100 million in the seven months ended last January. Arthur Martinez, Saks's vice-chairman, calls the report "highly speculative and

grossly inaccurate." He says he doesn't know why Heller stopped approving orders. "We are not going to release detailed financial information," says Martinez. "We are the best-capitalized retailer in America today."

FRETTING. Yet even suppliers who were shipping with confidence are nervous. "The longer you don't have information, you can't help but think equity has been pulled out, they didn't make their banking covenants, and the losses are more extensive than have been reported," says Leonard Rabinowitz, chairman of Los Angeles-based Carole Little for St. Tropez W, whose factor is Heller. (A factor is a credit company that buys manufacturers' receivables at a discount and then



ARE BIG LOSSES BEHIND THE ZIPPED LIPS AT SAKS?

retrieves payment from retailers.)

Rabinowitz sells million worth of app through Saks annu and counts Saks as of his best custom He's continuing to to Saks, but frets: "don't want to roll ou bed one morning find you have \$3 mi on the ledger that's collectable."

It wasn't suppose be this way. When S was bought by Bahr based Investcorp In national Inc. for \$1.5 lion in 1990, Seve Avenue said the A company had overp but was relieved th least one New Yo

based retail chain had deep pockets. vestcorp has a history of making lu tive investments in upscale retail such as Tiffany & Co., and was nowned for turning ailing establ ments around quickly. Plus, Saks long been known as one of the big "pencils" on Seventh Avenue—it w huge orders for suppliers' goods.

Since the takeover, Saks has take

COMPUTERS

DOES CONVEX HAVE A SHORT SOMEWHERE?

Bugs in its new supercomputer are giving investors the willies

When Convex Computer Corp. introduced its third generation of supercomputers three months ago, no one thought the job would come off without a hitch. But as Convex starts shipping its most profitable machines, unexpected bugs and a shortage of critical parts have made a trying transition even tougher.

Worse, Convex executives' high hopes for a quick fix aren't widely shared. Jittery investors fear the problems could slow shipments from the Richardson (Tex.)-based company and keep squeezing profits. Indeed, Convex is already losing money (chart). On July 26, the company announced a second-quarter loss of \$1.4 million, while sales dipped 3%, to \$50.5 million. In the next two days, Convex' stock sank 30%. "A lot of buyers just threw in the towel," says Jeffrey Canin of Montgomery Securities.

The stock's nosedive startled Convex executives. Although the loss is the company's first since 1985, they thought they had prepared Wall Street for the blow. Even Convex concedes it's unlikely to return to profitability until the fourth quarter. "It's been tough," sighs Chairman Robert J. Paluck.

Certainly, glitches aren't unusual. But Convex has suffered more than expected with its powerful C3 line of computers, which go for \$350,000 to \$8 million apiece. The exception: the low-end C3200, which hasn't had any problems since it went out the doors in May.

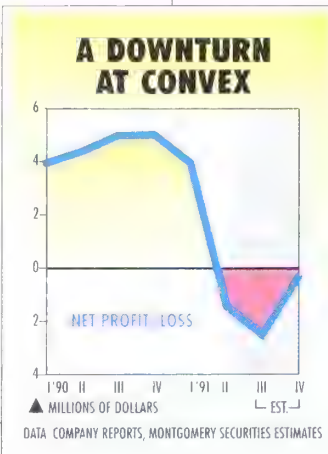
But the midrange

C3400, two units of which were shipped in June, is another story. It's suffering a pair of problems. For one, Convex finding it hard to lay its hands enough of the sophisticated computer chips it buys from Texas Instruments Inc. and Vitesse Semiconductor Corp. Vitesse supplies specialty chips made of silicon but of gallium arsenide. They're 2.5 times faster than the traditional silicon kind.

For another, the C3400 is based on reduced-instruction set computing (RISC) chip architecture, which should speed calculations. But Convex hasn't figured out how to keep the C3400 chips from impeding its memory-management systems.

When some applications are run, the RISC chip causes the C3400 to operate even more slowly than the C2, Convex' previous generation of supercomputers.

RED FLAG. Convex is modifying the C3400's software to sidestep the problem. Paluck maintains the machine is working fine for the applications such as image processing, for which it vs



of cost-cutting steps. To widen its base, it set out to slash some 700 jobs and expand its private-label operations. It abandoned the gift business and men's clothing, saying neither was profitable enough. The Saks discount store in Pennsylvania was thriving, and the company said it planned to open a chain of smaller Saks specialty stores. "Something was amiss. In July, In-Pop filed suit against Saks's former parent, British American Tobacco Co., although that BAT had overvalued Saks's equity. Meanwhile, the Manhattan store's traffic that Saks relies on heavily for the summer dwindled. And the company is taking a bite out of the retail trade, Saks probably isn't. How much, though, no one can say since the store won't reveal its sales. "Saks is really sticking it to the retail trade," says Alan Millstein, a retail consultant in New York. "The attitude is: 'Ship us or be damned, and we don't have to show you our numbers.'"

But factors say they're impatient with the zipped lips. They're demanding Saks disclose at least its balance sheet, income statement, and bank coverage. But with the retail biz on its ear, Saks caves in, many manufacturers are making the unpleasant choice of shipping to a potentially unstable customer or not yet another big pencil.

By Laura Zinn in New York

ically targeted. Yet its trouble has secondary applications—aircraft simulations, for instance—has a red flag to customers. Before it can build sales, "they'll have to see that the machine actually runs better than the C2," says analyst Tad Suki of Hambrecht & Quist Inc.

Shortage of gallium-arsenide chips grow worse with the high-end

Designed to compete head-to-head with boxes from supercomputer maker Ray Research Inc., the C3800 will be the industry's first to use gallium-arsenide chips throughout. Convex says the transition from Vitesse has been helped in part by design changes originally by Convex. Vitesse had no immediate comment on the supply problem.

Convex contends that all these hurdles will be overcome soon. He says Convex will meet its delivery schedules, including shipping the first C3800 in September, and the C3400s in the third quarter, and more of those midrange machines in the fourth quarter. The company's 1988 transition to its second generation of machines, Paluck notes, wasn't as sailing either. "In the end," he says, "C2 was a great success story." It looks as if a repeat performance is no mean feat.

Stephanie Anderson Forest in Dallas

INSURANCE

THE BLOOD FEUD BREWING AT JEFFERSON-PILOT

The insurer's management and dissident shareholders swap charges

Insurance companies are falling left and right these days, so it's hardly an ideal time to accuse an insurer of operating too conservatively. But that's exactly what a bunch of dissident shareholders are arguing in vowing a proxy fight for seats on the board of North Carolina life insurer Jefferson-Pilot Corp. "They've got so much excess capital, they could pay \$20 or \$25 a share in a special dividend and still be one of the safest life insurance companies in the country," says J. Craighill Redwine, a spokesman for the dissidents.

Only a few years ago, talk of a juicy asset flip like that would have quickly put Jefferson-Pilot in play. Not now. News of a July 24 Securities & Exchange Commission filing by the dissident group, which controls

2% of the company's stock, did nothing for share prices. Yet a vicious mud-slinging campaign on both sides is under way—and it promises only to get worse.

BURIED TREASURE? Jefferson-Pilot is probably best known as the syndicator of Atlantic Coast Conference basketball and football games. That's little more than a sideline, however, to its solidly profitable individual life and group health insurance lines. With \$4.4 billion in assets, Jefferson-Pilot remains essentially debt-free. It also wisely avoided stuffing its portfolio with junk bonds, and suffers only minor problems from its conservative real estate loans.

More important, it has built a \$1.4 billion stock portfolio that a spokesman acknowledges isn't all needed to backstop its long-term insurance obligations. That's the treasure the dissidents want to liberate. They argue that its value doesn't show up in the company's stock price, which has been idling for years.

A day after the SEC filing, the dissidents filed suit in federal court accusing Jefferson-Pilot of fraud. The allegation: A vaguely worded 1990 proxy statement duped investors into granting 70,000 shares of supposedly restricted stock to Jefferson-Pilot's 70-year-old chairman, W. Roger Soles, and five other top executives. The lawsuit contends there were

no performance or vesting requirements, so the grants amounted to a \$2.7 million windfall to "entrenched management, unrestrained by a compliant board."

Jefferson-Pilot says the allegations are untrue, and it's returning the fire. Speaking for Soles, Vice-President John T. Still III volunteers information about the 1970 seizure by federal regulators of a Michigan bank controlled by Donald

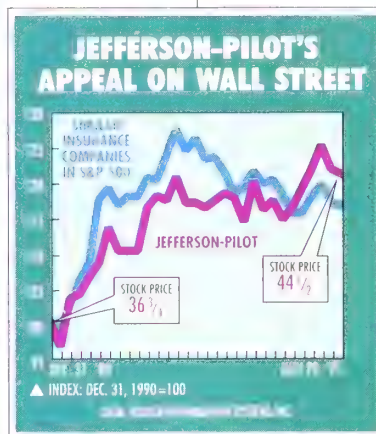
H. Parsons, the man now heading the dissident group. Parsons agreed to an SEC censure in 1973 that bars him from associating with broker-dealers or investment advisers. Still also speculates that Parsons' true motivation is settling a score for the family of his wife, Louise Price Parsons. Both her grandfather, Julian Price, and father, Ralph Price, once

headed the insurer, but her dad in 1950 was forced out by the board.

That, says Louise Parsons, is a smoke-screen. "The fundamental issue is that Roger Soles needs to retire," she says. "This company is stagnating and desperately needs new life breathed into it." Parsons adds that she adopted her activism after gaining full control of 300,000 shares of Jefferson-Pilot when her father died two years ago. In the last 15 years, she has overseen development of the Litchfield Plantation resort on South Carolina's coast.

Rhetoric aside, the Parsons group is raising an interesting question: Do shareholders have a legitimate right to demand that companies alter profitable operating strategies if they fail to boost stock prices? In this case, it looks as if an answer may be forthcoming. Jefferson-Pilot's stock has outperformed its peers in recent weeks (chart), but there's little likelihood of a major surge, given how much investors loathe insurers generally and the company's insistence that it won't be stampeded into a recapitalization. That means Louise Parsons, who told the SEC she has spent \$500,000 so far and is prepared to raise the ante to \$2 million, looks to be on her way to a nasty 1992 proxy fight.

By Chuck Hawkins in Atlanta



EDITED BY HARRIS COLLINGWOOD

TWA IS STILL FLYING—BARELY

► The scene on July 30 at the federal bankruptcy court in White Plains, N.Y., was tense. Some TWA creditors were prepared to repossess planes and equipment. Others lined up on the court steps ready to file to push TWA into bankruptcy. But when all appeared hopeless, Carl Icahn engineered a bailout. He appeased creditors, at least for now, with a debt-restructuring plan that calls for TWA to file a prepackaged Chapter 11 bankruptcy in early 1992. If the deal goes through, it will eliminate about \$1 billion in debt and leave TWA with \$400 million in cash once the restructuring is completed.

That's a big if, though. While some creditors are pleased with the plan, holders of notes collateralized by planes and engines say they've given Icahn until Aug. 5 to come up with a way to pay much of the \$65 million owed them. If he doesn't, they'll take their equipment back, grounding about two-thirds of TWA's fleet.

Even if creditors eventually sign on to Icahn's plan, TWA's survival isn't guaranteed. The slump in airline traffic and the continuation of discount fares may make it tough for TWA to continue to meet its financial commitments, especially since it will soon have to replace aging planes.

THE FLAME FLICKERS AT COLUMBIA GAS

► Unable to win concessions from either its bankers or natural-gas suppliers, Columbia Gas System on July 31 made good its threat to file for Chapter 11 bankruptcy protection. Executives say that the move should free it of old contracts to purchase gas at above-market prices. Those deals have bled the \$2.4 billion gas distributor.

Banks cut lines of credit for

the Wilmington (Del.) company in June when it suspended its dividend. Without the bankruptcy filing, Columbia was in danger of running out of money before it could strike deals with either bankers or suppliers. Columbia, which serves 15 Eastern states, signed some of the high-priced purchase contracts before deregulation and the current gas glut.

ENGINE INGENUITY IN JAPAN

► In late July, both Honda Motor and Mitsubishi Motor unveiled lean-burning engines that will increase fuel efficiency up to 20%—without sacrificing performance. And they did it by fine-tuning existing technology.

Honda will launch its new VTEC-E engine in Japan, the U.S., and Europe this fall, in a version of the 1.5-liter, three-door Civic hatchback. Mitsubishi will mount its MVV engine on a car coming out this fall, probably a version of the Mirage, but the company has no plans to export the model.

Both companies achieved the mileage and performance gains by redesigning the combustion process. The next task is to transfer the technology to larger engines, but for now, "it proves you don't have to scrap gas-burning engines and completely switch to something like methanol,"

DRESS BY DIOR, PURSE BY FIRESTONE

Where can a chic animal-rights activist put her keys and credit cards? What's a leather-loathing fashion plate to wear? Designer accessories produced from recycled inner tubes, of course.

They're available from Used Rubber USA, a venture set up by a couple of San Francisco artisans who scavenge junkyards and roadsides for their raw materials: tires and inner tubes dumped by drivers and cyclists. Used Rubber's bags, belts, skirts, and vests sell at boutiques and department stores in U.S. and Japan at prices from \$20 or so for a simple wallet almost \$200 for a briefcase. "A consumer does not have to sacrifice taste and style to be environmentally correct," says UR designer Mandana MacPherson.

Hepcats who sport an inner-tube belt don't even have to skimp on their sesame tofu and organically grown mustards. After all, rubber stretches a bit.



says Neal Doying, auto analyst for Baring Securities (Japan).

DID KENAMETAL AID IRAQ?

► Representative Charles Rose (D-N.C.) is investigating whether Kennametal Inc. of Latrobe, Pa., illegally shipped machine tools for military use to Iraq in 1989. The transaction was financed by Italian-owned Banca Nazionale del Lavoro in Atlanta, charged earlier this year with making more than \$4 billion in fraudulent loans to Iraq. Rose is probing BNL's activities.

The tools, valued at up to

\$300,000, were carbide tips for precision cutting and could be used to cut gun barrels or clear warheads, say Rose's staffers. A Kennametal lawyer who was fired after expressing misgivings about the order will testify about the deal before two House subcommittees in early August. Kennametal had no immediate comment.

A HASTY EXIT AT ALCOA

► Fred Fetterolf abruptly departed on July 30 as the No. 2 man at Alcoa. Fetterolf, 63, had been passed over for the top job four years ago. Instead, the board tapped outsider Peter O'Neill, then president of International Paper.

Fetterolf, a 39-year Alcoa veteran, and president since 1983, has been a strong supporter of O'Neill's strategy to refocus on the core aluminum business. But lately, he and O'Neill hadn't always seen eye to eye. Among the disputes: aluminum pricing, foreign joint ventures, and company executives. So Fetterolf's departure is one of few disruptions in the 55-year-old chairman's tenure. There's no sign of widespread unrest among senior managers.



THE MUCK FROM BCCI FLOWING INTO THE WHITE HOUSE

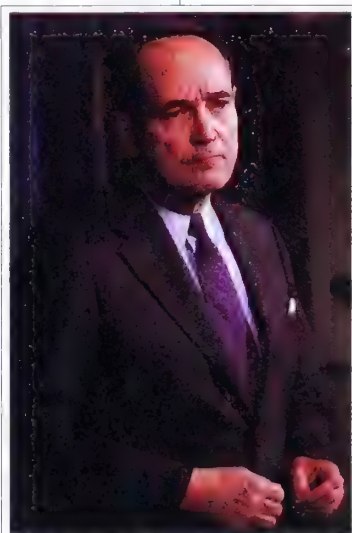
For more than two years, the Bush Administration has managed to avoid serious scandal. But now, just as the 1992 campaign is getting organized, the oil slick released by the sinking of the Bank of Commerce & Credit International is starting to wash ashore on George Bush's beach.

The BCCI mess is no Watergate. But it's starting to cause real damage. Two Bush nominations to top jobs and a recent Republican Senate candidate are threatened. And Democrats are poised to claim that Reagan-buzz has continued into the Bush Administration. White House aides admit they are not ready for the assault. "We're way behind the curve on this one," concedes one aide. The scandal broke while Bush was in a nonstop summitry, and staffers have not yet met once to discuss its implications.

First, the scandal flustered the opposition—since it also tainted First American Bankshares Chairman Clark Clifford and other prominent Democrats. But now the Democrats are on the move. Senator John F. Kerry (D-Mass.) has begun hearings into the affair. The Senate Foreign Relations subcommittee, and other committees plan to investigate.

The hearings will feature charges that Reagan regulators ignored BCCI's U.S. activities despite its shady reputation. "It all happened on Bush's watch," says Democratic Senator Rob Stroh. "BCCI reinforces a prevalent notion among voters that the Reagan Party closes its eyes when the wealthy get greedy." The Administration faces bigger perils than embarrassing leaks. The most immediate is the potential loss of Robert Gates, Bush's nominee to head the Central Intelligence Agency. Gates was already in trouble because of questions about his role in the 1986 Iran-*contra* affair. "This could be just straw," says Mitchell E. Daniels, former political director for the Reagan White House and now a vice-president

at Eli Lilly & Co. Gates, he says, is looking increasingly "expendable." A probe into allegations that the CIA used BCCI to transfer profits from arms sales to Iran to Nicaraguan *contras* threatens to renew charges that Bush has concealed the extent of his Iran-*contra* involvement. At a minimum, the CIA's admitted use of BCCI as a conduit for funds in covert operations may embolden Democrats to push for tighter reins on the agency in a major intelligence bill next year.



THORNBURGH: WAS JUSTICE BLIND?

William Taylor, Bush's choice to succeed L. William Seidman as chairman of the Federal Deposit Insurance Corp., may also be hit. Taylor, director of the Federal Reserve's bank regulatory operations, must explain how the Fed failed to uncover the secret ownership of First American by BCCI for 10 years. "If any major flaws in Taylor's judgment are uncovered, that will have consequences," says one Democratic Senate aide.

'TROUBLED TENURE.' An even bigger casualty for the GOP may be Attorney General Richard Thornburgh, who hopes to win a Senate seat in a Pennsylvania special election. His Justice Dept. has been busily denying allegations that it failed to investigate vigorously charges against BCCI and that it wouldn't assist a probe by New York District Attorney Robert M. Morgenthau. Appointed Senator Harris Wofford (D-Pa.) is ready to make this alleged foot-dragging a major campaign issue. "From now on, all the stories about

Thornburgh will be about his troubled tenure at Justice," says Wofford campaign manager James Carville.

The mess puts Bush in a rare position—on the defensive. "The BCCI scandal is symptomatic of an era under Reagan and Bush where excesses were winked at, where the wealthy and corporations were given a free rein," says Democratic pollster Stanley Greenberg. What a perfect line for a campaign speech.

By Douglas Harbrecht, with Paula Dwyer

AL WRAPUP

INEES

With opponents of Judge Clarence Thomas' nomination to the Supreme Court ready to launch an all-out attack, the Bush Administration is taking no chances in the confirmation fight. The White House has told all administration appointees to put in a letter for Thomas whenever they give a speech. Thus Transportation Secretary Daniel Skinner, on a visit to his home state of Illinois, compared Thomas to Abraham Lincoln: Both rose to the top from humble origins. But some officials are finding a seamless way to work Thomas into their appearances. In a recent speech on problems of pesticide

runoff, Environmental Protection Agency Administrator William K. Reilly found himself saying: "And from the storm over Judge Thomas, let me now turn to storm water..."

DISABILITIES

Employers are worried about a key omission in the new regulations for the Americans with Disabilities Act. Companies fear the law leaves them open to suits if they try to reduce health coverage for specific illnesses, such as AIDS. They were hoping for guidelines in the regs. But the Equal Employment Opportunity Commission, after considering the issue, decided to hold off rules pending further study.

INVESTIGATIONS

Evidence that the 1980 Reagan campaign interfered in the release of hostages from Iran in order to hurt President Carter's reelection chances remains scanty at best. But the rumors won't die, and House Speaker Thomas Foley (D-Wash.) has agreed to authorize a congressional inquiry into the matter. Even so, Foley remains very skeptical about the charges: He plans to state publicly that he sees nothing to suggest that George Bush, then the Vice-Presidential nominee, had any involvement in putative secret meetings between Reagan-Bush campaign aides and Iranian representatives.

PRESIDENT SALINAS: 'MY PEOPLE ARE IN A HURRY'

Mexico's leader talks about free trade, geopolitics, and poverty

Mexico's 43-year-old President, Carlos Salinas de Gortari, approaches the midpoint of his six-year term on a roll. He has refinanced Mexico's debt, rewritten foreign investment rules, and sold state-owned companies. What's more, he has put the country on a fast track for a Free Trade Agreement with the U.S. and Canada.

Under Salinas, inflation is down and Mexico's economy is growing faster than its population. Politics, however, remains mostly a one-party affair. Indeed, Salinas' PRI (Institutional Revolutionary Party) appears primed to steamroll a fractured opposition in August's congressional elections.

Recently, Salinas met in Moscow with Soviet President Mikhail Gorbachev. Later, in Guadalajara, he hosted a meeting of 23 Latin heads of state, including Cuba's Fidel Castro.

BUSINESS WEEK Editor-in-Chief Stephen B. Shepard met with Salinas at his official residence, Los Pinos. In a 45-minute interview with Shepard and Mexico City Bureau Manager Stephen Baker, Salinas described how he is trying to pull Mexico from the Third World toward the First. Some excerpts follow:

Q You have made enormous progress in three years. What are your goals for the next three years?

A Mainly, to consolidate the restructuring of the economy. The Free Trade Agreement [FTA] with Canada and the U.S. is very important because it will allow us to grow faster. But we are not waiting for the economic recovery to produce social results. We are deliberately promoting social programs. We've seen in the past how recoveries are impressive in statistical terms. But they leave behind too many people in poverty. I don't want that to happen with us. That's why our social programs are a huge priority. But there are some uncertainties.

Q What are they?



**"We're in for a very tough battle"
for scarce capital**

A Mostly, the international situation. First, the need to arrive at a positive solution in the General Agreement on Tariffs & Trade [GATT] negotiation. That is, to have general rules to avoid trade wars. Second, the scarcity of capital in the '90s, what with the cost of financing central Europe and German unification, Asian development, even the U.S. recovery. It means that we're in for a very tough battle for scarce financial resources. And last but not least, the uncertainty in the Soviet Union. That

worries me a lot. It's still a nuclear power, a superpower, and the viability of economic reform is not clear, and therefore our capacity to respond to special demands. Anything that happens there on a grand scale could have a tremendous effect on Europe and the rest of the world.

Q Various regions are moving into trading blocs. Does that undermine GATT?

A They could undermine GATT if these blocs were to become fortresses. That would be a tremendous mistake. So we must make it very clear in our FTA that Mexico, the U.S., and Canada should be an open region. We hope that Europe in 1992 will have the same attitude, as well as Japan and the Asian countries.

Q Would Mexico pressure low domestic content rules in the FTA?

A Not necessarily, because we want goods to be produced here so that employment increases. My interest in the FTA is to be able to grow at a fast rate—the only way that I can respond to the interests of the 82 million Mexicans today and the almost 2 million that are added every year. So I need jobs here. My people are in a hurry. As jobs will be created if domestic content is high.

Q Why has Japanese investment in Mexico been small to date? Are they waiting for an FTA?

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...ages have been held
too?

...ages have increased
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basis and in relation
productivity.



Castro "knows he's at his worst moment economically"

Q That has happened two years in a row?

A In 1989 and 1990. If we reach 15% inflation, we will certainly witness a third year in a row that wages increase in real terms. We want higher wages in Mexico on a sustained basis.

Q Do you see much change coming in the oil industry?

A We hope to produce more. In terms of who produces it, no change. The constitutional requirements [that Mexico own

others. Quite a critical press. An open society. What I want is to upgrade what we have. It seems to me that the Soviet Union is in the process of changing the fundamentals. It's very different. I found Gorbachev a determined man. We had a chance to talk for four hours.

Q Should he have put economic reform before political openness?

A I asked him that question. He said he wanted to further *perestroika* first, but that the system was very closed against economic reforms. So he let political reform proceed. Now, he doesn't have economic reform, and he has tremendous political instability.

Q Do you get a sense that he regrets that he didn't move more quickly on the economic side?

A He didn't mention it like that. The problem is that they never had a mixed economy. When you want to privatize, you must first ask yourself whether you have private businessmen to whom to sell. Well, they don't have any. In Mexico, we knew that we had a very strong private sector with the capacity to innovate, the resources to buy, and the attitude to accept foreign



"We must make it very clear in our FTA that Mexico, the U.S., and Canada should be an open region"

investors. But in the Soviet Union, who has the resources to buy those companies? Who has the skill to manage them? It is not only a question of will but of building a new generation. And that takes time. The question is: Do they have it?

Q *What is your sense of the recent Guadalajara summit of Latin American leaders?*

A It was a very successful meeting. First and foremost, we were all there. For the first time in history, the heads of state of every Spanish and Portuguese country in Latin America and Europe came together. That in itself was a political statement. Next was the recognition of regional trends—the reform of the state, integration, liberalization, promotion of the private sector, response to social demands, the process of democratization.

Q *What was the attitude toward the U.S.?*

A Oh, I would say it was respectful, and I would even say that the relationship that the Bush Administration has built with Latin America is very positive. It was not a reunion against anyone. It was a reunion for the integration of Ibero-America. It was a dream for 200 years. And slowly, it can become reality if we are pragmatic enough to put rhetoric aside.

Q *Is Fidel Castro isolated? Do you see much change?*

A I would say that he presented his ideas as he usually does. Although in the closed meetings, his speeches were moderate and with the desire to be part of the region... He knows that he's at his worst moment economically. Several of us asked him: "If you make a speech in which you denounce capitalism and private property, how do you expect to stimulate foreign investment?" They asked him about consistency. Well, he will just have to respond on his own terms.

Q *Where could Mexico be by the year 2000?*

A If we maintain fiscal discipline, if we persevere in our macroeconomic strategy, if we consolidate the opening of our economy, if we fulfill the restructuring of our microeconomy, [then] by the end of this decade, we can certainly aspire to be one of the emerging industrialized countries. If.

GERMANY

A CHALLENGER FOR GERMANY'S HEAVYWEIGHT BANKING TITLE

Insurer Allianz picks a fight with Deutsche Bank by buying into a rival

Europe's financial mavens are having a hard time getting to the beach this summer. A series of financial bombshells are keeping their eyes glued to their quote screens. The latest went off on July 30 when Germany's Allianz, the Continent's biggest insurer, announced that it had a 23% stake in Dresdner Bank.

Over the past decade, Allianz CEO Wolfgang Schieren has extended the company's global reach in a frenzy of deals with banks and insurers. Now, with a major share in Germany's second-largest bank, Allianz suddenly looks like a bona fide challenger to Deutsche Bank as the nation's—and Europe's—leading financial colossus. "The power center of German business is not Deutsche Bank but Allianz," says Guido Schmidt-Chiari, chairman of Creditanstalt-Bankverein, Austria's leading bank.

JOCKEYING. In addition, the presence of two powerhouses, Deutsche Bank and the Allianz-Dresdner combo, will make it tough for outsiders to enter the German financial markets. Dominance of their lucrative home turf will likely provide these German institutions with the springboard they need to expand throughout Europe.

Schieren is jockeying for the lead in building a financial supermarket to cash in on Europe's soon-to-be-borderless banking and insurance markets. He envisions a network of banks and insurance companies that will funnel clients to each other. He thinks this strategy—known as "Allfinanz" in German—will allow Allianz to steal a march on Deutsche Bank not only in Germany but also in the race for Europe's 320 million potential clients.

While Schieren's moves have clear business logic, he is also driven by personal ire aimed at Deutsche Bank, which holds 10% of Allianz. His grudge dates to a spat with the Frankfurt bank's former CEO, Alfred Herrhausen, who was assassinated by terrorists in 1989. When the aggressive Herrhausen decided in 1988 to set up an in-house insurer to compete with Allianz, a livid Schieren stomped off Deutsche Bank's board.

To defend Allianz' 16% share of German insurance premiums from Herrhausen's raiding, Schieren quietly struck deals with Dresdner to peddle Allianz policies through its tellers' windows. Munich's Bayerische Hypotheken- und Wechsel-Bank had been operating locally since 1919. He cemented the arrangements by buying a 24% stake in the Munich bank and agreeing with Dresdner to buy up each other's shares in the market. Dresdner now holds 10% of Allianz worth \$2.2 billion.

RAW MUSCLE. Schieren had also been quietly buying Dresdner shares before revealing the huge \$1.7 billion holding. When he retires Oct. 2, the 64-year-old will pass on to his newly designated successor, Henning Schulte-Nölde, an Allianz with an estimated \$230 billion in



ALLIANZ CEO SCHIEREN: THE BANK-INSURER COMBO WILL BE A SPRINGBOARD TO EUROPE

investments, and holdings averaging 10% of every listed German company. That's more raw financial muscle on tap than even Deutsche Bank can muster.

While Allianz can't run Dresdner under German antitrust laws, most observers think that Schieren has placed Dresdner boss Wolfgang Röllner in debt by giving him antitakeover protection from Europredators such as France's state-owned banks. Röllner's side of the bargain is presumably to follow Allianz' lead in the insurer

ss. "Allianz is binding banks group. It's a smart move be- it can stop Dresdner from doing me as Deutsche Bank in insur- says Christian von Budingen, executive officer at Frankfurt bank Schröder, Münchmeyer, t & Co.

Allianz-Dresdner bank-insurer al- follows a pattern that's becoming r. Lloyds Abbey Life PLC, created by Britain's Lloyds Bank PLC and mer Abbey Life Group PLC, was

an early model that has since been wide- ly imitated across Europe.

Some of the pioneers belittle the Ger- mans' financial savvy. "Their product creativity has been limited," says Chris- topher Wiscarson, Lloyds Abbey's direc- tor for Europe. What remains to be seen is whether Germany's undoubted finan- cial muscle will win out over others' sup- posed finesse.

By John Templeman in Bonn, with Richard A. Melcher in London and William Glasgall in New York

THE STOCK SCANDAL AT WON'T GO AWAY

Tokyo bigwigs try to squelch it, tempers flare at home and abroad

as a rude awaken-
Unfolding their
ning newspapers
y 29, horrified Jap-
executives found
company names on
st: the 228 corpora-
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or \$930 million in
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the details at a
conference.

this disclosure,
se officials, includ-
ayweights in the
Democratic Par-
hoping to sweep
s stock scandal
ight. But Tokyo's
brokers are not yet
clear. A Diet upper
probe is set to be-
g. 2 seeking more
e of broker reim-
nts to clients.
g Four have yet to
details on pay-
ade after Mar. 31,

then the stock market plummeted
and at least six smaller brokers
dy to name names of those they
rsed for \$254 million.

UT. The revelations are also stir-
U.S. reaction. Charles Stevens,
orney at Coudert Brothers in To-
ys three of his U.S. clients are
ing to sue Japan's brokers.
are established pension and mu-

tual funds, which are annoyed that their
Japanese counterparts got reimbursed
for losses while they did not," he says.
Although U.S. officials are lying low,
they are gathering ammo for upcoming
talks on barriers to doing business in
Japan. "The scandal convinces us of the
validity of our agenda," says one offi-
cial. "It increases our leverage."

The crisis is rattling Japan's blue

chips, the main recipients of broker pay-
offs. "I'm pretty worried about how our
foreign customers will react to our in-
volvement in this," says a managing di-
rector at Hitachi Ltd., which received
\$16 million. Both Keidanren, Japan's big
business association, and the Ministry of
International Trade & Industry are
launching investigations.

As shaken as they are, most compa-
nies claim they don't remember getting
reimbursed. Daiwa Securities Co. says it
paid Nissan Motor Co. \$12 million to cov-
er stock losses, but Nissan officials say
they first learned of it in the newspa-
pers. "There's no indication we were
compensated for losses," says Kane-
mitsu Anraku, general manager for fi-
nance at Nissan. But many analysts re-
main unconvinced. "The amount of
compensation was huge," says Ryukoku
University professor Hiroshi Okumura.
"It's hard to imagine they didn't know."

CHEAP INTEREST. For business, more is
at stake than payoffs. Brokers' subtle
promises of steady returns helped fuel
Japan's capital-investment drive in the
late 1980s. Protected by safety nets, in-
vestors pumped money into fund man-
agement accounts. Peaking at around
\$250 billion, these funds drove the mar-
ket higher, enabling companies to raise
capital at rates of just 1% or 2%. Now,
the cost of capital is rising, in part be-
cause investors are wary of stock trades
without any guarantees.

While business feels the heat, the LDP
believes the pressure is off. Since there
are no politicians on the list, it now ap-
pears that former Nomura Securities
Chairman Setsuya Tabuchi will not tes-
tify before the Diet. Party leaders wor-
ried that he might expose the dark side
of Japan's campaign financing. To pack
campaign coffers, top politicians are
widely suspected of having bought
stocks just before the Big Four moved
to drive up their prices. "We all feel a
great sense of relief," says Tetsuo
Kondo, LDP finance committee chairman.

It's not over yet. Prime Minister To-
shiki Kaifu and LDP Secretary General
Keizo Obuchi want an independent en-
forcement agency similar to the U.S.
Securities & Exchange Commission.
Powerful Finance Minister Ryutaro Ha-
shimoto is maneuvering to preempt such
action by setting up an enforcement
group within the ministry and revising
securities laws. "They've circled the
wagons and want to move on to some-
thing else now," says economist Ken-
neth S. Courtis at Deutsche Bank Group
in Tokyo.

To the ministry's delight, the stock
market snapped back after the list was
revealed. But ever since it broke nearly
two months ago, the scandal has proven
to be very resilient, too.

By Ted Holden in Tokyo



TOKYO'S FINANCIAL DISTRICT: "THEY'VE CIRCLED THE WAGONS"



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DE KLERK STUMBLES— AND THE ANC STANDS TALLER

Just weeks after winning his biggest international triumph, South African President F. W. de Klerk has suddenly lost political headway at home. De Klerk was riding high when President Bush decided on July 10 to reward his steps toward dismantling apartheid by scrapping U.S. economic sanctions. But now, disclosures that security agencies in de Klerk's government secretly financed Zulu Chief Mangosuthu Buthelezi's Inkatha Freedom Party, the conservative rival of Nelson Mandela's African National Congress, have badly dented President Klerk's reformist mantle. The likely result will be to bolster the ANC politically and strengthen its drive for an interim government to rule during the transition from apartheid to nonracial democracy.

In an effort to contain the political damage, de Klerk on July 29 demoted Defense Minister Magnus Malan and Law & Order Minister Adriaan Vlok, who controlled the military and police. Then, he replaced them with more liberal Cabinet colleagues. He also pledged to appoint a group from the private sector to advise him on covert activities. De Klerk said he will soon name a judicial commission to probe the security forces' alleged role in violence that killed 2,000 South Africans in the past year.

WATER FORCE? These moves should help cushion the blow to de Klerk. But the evidence of covert political activity reinforces the ANC's argument that the ruling National Party can't be trusted to guarantee fairness in the process of reshaping South Africa. Up to now, de Klerk has managed to sidestep the ANC's demand for power-sharing by taking a series of steps to remove key features of apartheid. But on July 30, he said he was ready to start negotiations with all parties, with "transitional arrangements" as the top agenda item. The talks are likely to start soon, although the ANC insists that the government first release all prisoners that the ANC classifies

as political. It also will wait to see what de Klerk does to end the violence.

So far, there is no clear evidence of collusion between Pretoria and the Inkatha Freedom Party in stirring the grassroots mayhem. But the disclosures of the government funding for Inkatha have stirred even the white Establishment. The liberal opposition Democratic Party and moderate newspapers are now more ready to believe ANC charges that a sinister "third force" linked to security agencies has provoked the clashes.

Besides pushing de Klerk to yield on issues such as power-sharing, the scandal may also have international repercussions. It seems likely to deter efforts by President Bush to scrap the Gramm Amendment, which requires the U.S. to veto International Monetary Fund loans to Pretoria. And it may strengthen the resolve of U.S. states and cities to continue their own anti-apartheid sanctions. "I think it will give people pause as to the intention of the South African government to allow a democratic process," says Miloanne Hecathorn, the Oakland (Calif.) official in charge of implementing that city's sanctions.



WERE INKATHA-ANC CLASHES PROVOKED?

The biggest loser, though, is Buthelezi. In the past, he and Inkatha were seen by many white liberals and executives as a moderate anti-apartheid, antisocialist alternative to the embattled National Party and the ANC. Now, although Buthelezi retains support among his Zulu constituency, the exposure of his conniving with security forces has probably destroyed his hope of attracting a wider following. More and more, the struggle to reshape South Africa looks like a face-off: de Klerk and the National Party, still wielding the levers of official power, vs. Mandela and the ANC, with a strengthened claim to speak for the country's black majority.

By Alan Fine in Johannesburg

GLOBAL WRAPUP

INDIA

Chalk up another casualty of the new world order. Since the 1950s, Moscow and New Delhi have enjoyed a special relationship with close political and economic ties. But the superpower rivalry that aligned the Soviets and India against the U.S. and Pakistan has waned. Now, market economics is undermining Indian-Soviet trade.

That will become clear in talks this month aimed at phasing out an outmoded "rupee payment arrangement" that propped up trade between the two countries. The Soviet Union was India's second-biggest trading partner after the U.S. last year. But Moscow's

overvaluation of the ruble against the rupee skewed the trade balance in India's favor. Now, the all-but-broke Soviets owe some \$800 million to Indian suppliers that they can't repay.

Both sides want to shift dealing to a hard-currency basis. But that will mean less trade. Already, the Soviets are looking to South Korea and others for products from TV sets to autos that they have been getting from India. New Delhi's state oil company, meanwhile, is looking to Indonesia and Brunei as Soviet oil exports dwindle. About the only party lobbying to keep the trade pact is India's Defense Ministry. It has been buying MiGs and other arms with funny money from Moscow.

CANADA

A famous Canadian multinational—Varity Corp., formerly Massey-Ferguson Ltd.—is moving from Toronto to Buffalo. That seems sure to fuel Canadian fears of losing industrial gems as companies restructure under the U.S.-Canadian Free Trade Agreement. Other companies have shifted jobs south of the border, but Varity is going all the way, relocating its headquarters to the U.S.

Canadian politicians decry the July 30 decision, citing Ottawa's substantial aid to Varity in the 1980s. But CEO Victor Rice responds that most Varity plants are already in the U.S.

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Hard Disk Drive	30MB	60MB	60MB	120MB	120MB
LCD/Size	Backlit 8.85"	Backlit 8.85"	Backlit 8.85"	Edgelit 10.7"	Edgelit/10.7"
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FASHION



BROOKS BROTHERS HOPES TO GAIN MARKET SHARE BY KNOCKING \$100 OFF ITS TOP SUIT

THE SUIT MARKET IS COMING APART AT THE SEAMS

Looser dress codes, recession, and sticker shock stymie sales

Our apparel is always in evidence and affords an indication of our pecuniary standing to all observers at the first glance.

—Thorstein Veblen, *The Theory of the Leisure Class*

Veblen's theory may need updating. Just consider what's happening to the suit, that once reliable guide to a man's standing. Brendan Byrne, Harvard University law graduate, former New Jersey governor, and partner in the Roseland (N.J.) law firm of Carella Byrne, recalls a recent board meeting at which he discussed clothes with the former chairman of a large consumer-products company. Both wore sports jackets and slacks, says Byrne. "And this guy said he takes the brass buttons off his blazer and puts on regular buttons so nobody will notice he's not wearing a suit."

Byrne is, well, following suit. He now buys one suit every two years, down from two a year. His favorite is one from 1968. "The lapels are a little narrow, but nobody notices," he says.

Suitmakers sure are noticing. In 1990, domestic and foreign manufacturers made about 15.5 million men's and boys' suits for the \$2.9 billion U.S. retail market, down from 18.4 million in 1989. Based on interviews with 35,000 consumers, market researcher MRCA Information Services projects that from January through May, 1991, consumers bought \$796 million in men's and boys' suits—down 9% from the same period in 1990.

The economy's slump has obviously hurt. And rising wool prices and better demand drove suit prices up 30% in the late 1980s, just before the recession. "All those young guys with a lot of dollars in the '80s see friends out of work, and

now tailored clothing is the last thing anyone's mind," says Norman Fryer, chief executive of Greif Companies, suitmaker for the likes of Perry and Ralph Lauren.

Recessions aside, the trend has been mostly down since before 1979, when more than 25 million suits were made for the U.S. market. "There's a negative trend that goes back to the '70s," says Stig A. Kry, chairman of retail consultants Kurt Salmon Associates. Why the lengthy unraveling? For starters, there's the general decline of formality. Says William V. Roberti, chief executive of Brooks Brothers: "My dad had two or three suits, and he was a factory worker. He dressed up on a Sunday. I looked like a million dollars. People don't dress like that anymore."

Then there's the casual style work its way into office life. A number of California securities firms have declared Friday a "suit-optional" day. So has the New York office of law firm Orrick, Herrington & Sutcliffe. And almost every day is suit-optional for the growing ranks of the self-employed. As a marketing executive at Prime Computer Inc., Dave Bryant "had to wear a uniform every day—and that was a suit." Not as a partner in Carlyle Group, a foreign person consulting business in Framingham, Mass., he's more likely to wear Dockers pants and a polo shirt.

For many in the tailoring trade, such habits spell trouble. And there's little export business to pick up the slack. One well-known manufacturer bluntly puts it: "The story is that the men's suit business is going into the toilet." For example, Hartmarx Corp., maker and tailor of such labels as Hickey-Freeman and Hart Schaffner & Marx suits, lost \$62 million last year and announced closings of 65 stores and 7 factories.

'UNDER SIEGE.' Local retailers have also suffered. Homer Reed Ltd. has closed Denver executives for 40 years. Now says President Homer Reed, he sells many suits at three stores combined. He once sold in his single downtown outlet. "It's breaking my heart," says Reed. "Customers come in and say: 'Homer,

I've bought my last sport coat from you. If I wear a sport coat to a party, I feel overdressed.' In the New York City area, George Kosack, CEO of off-price retailer NBO Stores Inc., figures suits are down to 25% of his business from more than 30% in 1989. "The suit industry is under siege, and this is not a one-year phenomenon," he says. Even Kosack admits: "I only wear suits when I have to."



Apparel makers do see bright spots. Orders are up 4% for spring 1992, and it's the first significant uptick we've seen in four seasons," says Elbert O. Lind, president of Hartmarx. Hand figures that retailers have used up inventories and expect some rebound.

In the meantime, some retailers and apparel makers have decided to provide a suit to go around the deepest pockets. Norman Hilton, a Linden (N.J.) manufacturer of pricey off-the-rack suits, is now in the "bespoke" business making suits to order—starting at a steep \$1,100. Bergdorf Goodman Inc., the chic women's-apparel retailer, opened its men's store last year for "the man who goes to all the best hotels, the clubs," says Bergdorf Chairman Ira Neimark. Bergdorf's Armani suits, for example, regularly retail for \$2,000 or more—although on a recent summer day these suits had discount tags of \$1,025. Neimark sees first-year sales about \$3

million short of his \$40 million plan.

Other retailers are pinning hopes on a dose of Eurostyle. Barneys New York expects to sell roughly 25,000 suits this year—about the same as 1990, says Peter Rizzo, senior vice-president in charge of menswear. But he sees good growth in suits with a less structured Armaniesque look and a \$600-to-\$800 price tag. "Those are moderate price points today," he says with a laugh. Hartmarx, too, has new European-cut lines from designers Karl Lagerfeld and Krizia.

MIX AND MATCH. At the other end of the market, bargain outlets for men's suits are proliferating. Then there's something that might be called the build-your-own-for-less suit. Sears, which abandoned its own house-label suit business, has reentered the fray with jackets and matching pants sold on separate racks. That way, customers who don't fit into a single-size suit can mix and match. Sears' "finished suiting separates" cost

\$45 for pants, \$100 for jackets. Similar "suited separates" are garnering double-digit sales gains at J.C. Penney Co. Even preppy Brooks Brothers, whose earnings were down 57%, to \$10 million, in its last fiscal year, is now selling such separates, which usually go for \$395 per combination. Brooks reports that this "Wardrobe" line already represents 30% of its suit business.

Still, Brooks's Roberti knows the business will remain tough: "The suit market as a total universe is getting smaller." His business, he says, is holding steady. He's hoping that lowering the price of a top Brooks suit by \$100, to \$795, will help gain share in a declining market. In the suit business, that's probably the smartest way for a company to preserve its pecuniary standing.

By Laura Zinn in New York, with Sandra Atchison in Denver, Stephanie Anderson Forest in Dallas, and bureau reports

TIES ARE DOING MORE OF THE TALKING

Sam Singer is perfectly happy to don black tie and cummerbund for a night at the opera. The San Francisco-based political consultant used to buy five suits a year. Now that he's the father of infant twins, he buys one—on sale. But don't even suggest that he stop adding to his collection of more than 100 neckties—"very dressy at hip"—and often running \$85 and up. "When I barbecue, I wear tie," he says. "It's a manly thing to do."

Suitmakers may be weeping in their wool, but it seems many men still want snazzy avatars. "Selling ties today is as easy as falling off a log," says John H. Romanow, marketing director of tie manufacturer Wemco Inc. The New Orleans necktie maker projects 1991 revenue up 25%, to \$62 million. With ties, says Romanow, "men can revamp wardrobes without spending \$300."

Ed Larkin, a young attorney at the New York firm of Donovan Leisure, agrees. He buys suits on discount, but "I sort of believe that when you see a tie you like, you buy it right then." The Neckwear Association of America figures 1991 retail necktie sales will hit \$1.4 billion, up 5% from last year. And many retailers love the action at their tie counters. Neckwear is very good. Real good," says Peter Rizzo, senior vice-president at Barneys New York.

It isn't just the dress-for-success-for-less crowd who are snapping up more ties. New customers include teenage boys who wear ties with oversize shirts. "People who never have to wear a tie are buying them," said Daniel Glynn, marketing director at Structure, The Limited Inc.'s new 179-store casual menswear chain. "It's fashionable to wear ties with jeans and shorts." After

freshen up older suits with such accessories as enamel cuff links and, naturally, \$25 to \$99 ties. "That's the way it should be if they've bought good clothing and paid a high price for it," says Grodd. Paul Stuart also sells such tie accessories as a \$67.50 silver tie bar with a fishing fly embedded in crystal.

For neckties, this up cycle is especially vibrant—in more ways than one.

"Florals," the industry tag for ties featuring gorgeously colored flowers, swept through the stores last year. Now, tiemakers say the next big look is the 1950s-style geometric print. As for more staid styles, "the striped tie died," says Katie Smith, president of Mulberry Thai Silks Inc., a San Anselmo (Calif.) startup that sells handwoven silk ties from Thailand.

The rise in ties isn't lifting all boats, though. The Tie Rack, a \$100 million chain of stores in nine countries, sees its U.S. tie sales flat at \$8 million this year, partly because of recession and lower sales of its traditional ties. Now it's offering ties sporting reproductions of paintings by Van Gogh and Canaletto.

Are these conversation pieces just another faddish indulgence? Not according to Singer. He sees them as a legacy for his twin sons: "These ties are a reflection of the fancy of the season they were born."

By Alice Z. Cuneo in San Francisco



BARNEYS NEW YORK IS SEEING PLENTY OF NECKWEAR ACTION

starting with a few dozen styles of cotton ties last year, Structure stores are now carrying hundreds of varieties in both cotton and silk. The Gap Inc. will sell neckwear this fall as well.

GEOMETRIC PRINTS. Of course, most necktie wearers are still businessmen. Clifford Grodd, owner of Paul Stuart Inc., an expensive men's retailer in New York City and Japan, sees plenty of Wall Street types coming in to

CEO WANTED. NO INSIDERS, PLEASE

More companies are turning to outside talent to rescue them

It's something of a corporate trend: Outside CEO. During the past three months, a number of high-level executives have bolted from some of America's premier corporations. William Lowe has moved from his post to join Gulfstream Aerospace as its heir apparent. Then Stanley C. Gault, who had just left Rubbermaid on May 1, agreed to take the top spot at Goodyear Tire & Rubber. Then in July, General Electric Vice-Chairman Lawrence A. Bossidy vaulted over the wall and joined Allied-Signal as CEO.

Just a bunch of fast-trackers sprinting ahead? Perhaps. But they're hardly alone: A growing number of companies are turning to outside talent to lead them forward. Since 1988, some 30 executives recruited from outside have been placed as CEOs at such companies as General Dynamics, Gerber Products, Campbell Soup, and USF&G.

TOUGH CALLS. Why are so many companies looking for that perfect stranger? The recession is clearly part of the answer. Hard times call for hard decisions—ordering massive layoffs, slashing dividends, icing pet research and development projects. The tough calls may come more easily to an unsentimental outsider than to an executive who has spent his career at the company.

But boards aren't just looking for cold-eyed hatchet men. An executive from a rival within the same industry can offer a different slant on the market, links to new suppliers and customers, or approaches. An outsider from a completely different business can often bring an even fresher eye to a company and its woes, since he or she starts with few preconceived notions of how things have been granted. Either way, the outsider can enliven an ossified corporate culture with new ideas—and new blood, since many bring along

their own special team of managers.

Or so go the arguments in favor. On the other hand, an outsider may find himself totally at sea in a new corporate berth. The newcomer may be forced to spend so much time learning industry fundamentals, familiarizing himself with operations, or feeling his way through the political maze that he has little chance to take decisive action. And the arrival of an outsider may drive away a company's seasoned hands. Says Wharton School Professor Stewart Friedman, author of an upcoming study on CEO outsiders: "Outsiders tend to be more disruptive and cause more turnover of other top managers than insiders."

For good or ill, more companies will have to cope with such disruption. Survey data of executive migration at big companies show the trend is growing. The percentage of outsiders has edged up steadily in the past three years, after falling a bit in 1986 and 1987. This year, it's estimated, outsiders will represent 28% of all newly hired CEOs at the 385 companies polled by Eugene E. Jennings, professor emeritus of management at Michigan State University's Eli Broad School of Management (chart). That would be a 33% increase from 1988 and match the 28% set in 1985—a year when the takeover craze resulted in an unusually large number of outsiders assuming the throne.

The case of Campbell Soup Co. illustrates the potential benefits—and at least one drawback—to this trend. Bur-



dened by inefficient plants, bloated costs, and a clutch of unprofitable products, Campbell's earnings grew ranked ninth in the industry during the '80s. Even so, then-CEO R. Gordon McGovern, a 33-year Campbell vet steeped in its paternalistic culture, resisted wielding the ax.

After McGovern retired under pressure in 1989, the board recruited David W. Johnson from Gerber Products Co. Johnson soon did what McGovern long avoided: He trimmed Campbell's 55,400 member work force by 21%, shuttered or sold 20 plants worldwide, and yanked unprofitable brands. "The person who coming from the outside into a turbulent or needy situation is like a hellfighter," Johnson says. "He's the one who's digging wells that are out of control."

Campbell's profit growth is now No. 1 in the industry. Earnings from continuing operations in the fiscal year ended July are likely to jump 41% to \$44 million, on \$6.8 billion in sales, figures White First Securities Inc.

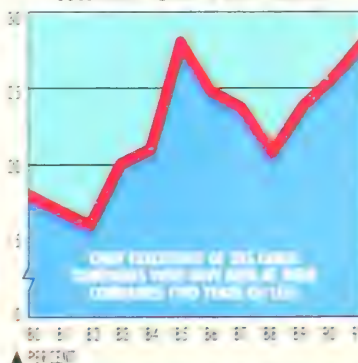
But there has been downside, too: Johnson's arrival has prompted at least one valued top executive split. Campbell's Chi-

THE OUTSIDERS...

A SAMPLING OF CEOs RECENTLY HIRED FROM OUTSIDE

NAME	NEW COMPANY	OLD COMPANY
LAWRENCE BOSSIDY	ALLIED-SIGNAL	GENERAL ELECTRIC
STANLEY GAULT	GOODYEAR	RUBBERMAID
WILLIAM LOWE	GULFSTREAM	VEROY
NORMAN BLAKE	USF&G	HELLER FINANCIAL
HOLLIS HARRIS	CONTINENTAL AIRLINES	DELTA AIRLINES
DONALD RUMSFELD	GENERAL INSTRUMENT	WILLIAM BLAIR & CO.

...ARE ON THE RISE





Financial Officer Edwin L. Harper resigned on July 27, lamenting that he had not passed over for the CEO job.

Similarly, Aluminum Co. of America's Paul H. O'Neill is widely credited with refocusing the company on its core aluminum business in the four years since he joined Alcoa from International Paper Co. But he, too, illustrates some

of the risk of bringing in an outsider. O'Neill had judged the commodification of sheet aluminum when he stubbornly tried to hold up prices in late 1989, cost-

Alcoa some \$100 million in sales. And his decision over that and other decisions led to the resignation of President C. Fred Fetters' unexpected resignation announcement on July 30.

Another outsider is delivering a tooth-pulling shakeup at USF&G Corp. Norman Blake Jr. took over as CEO at the troubled insurer last November after leaving Chicago-based Heller Financial Corp., a corporate lender. USF&G lost \$569 million last year, thanks to heavy losses in its property-and-casualty underwriting business, reserves for possible losses in junk-bond and real estate investments, and a restructuring.

Although Blake had little experience in insurance, he moved decisively. On his

first day, he met with top executives and told them that he didn't believe in the "arrogance" of corporate perks. He shut down USF&G's ritzy executive dining room and started eating with employees in the company cafeteria.

He also shattered any hope that USF&G's coddling ways would continue. Blake laid off 25% of USF&G's work

force—the first such reduction in the company's 95-year history. He cut the dividend from 73¢ to 5¢ per share. Such moves were a real jolt. Says Blake: "This crazy man from Chicago shows up, and the first thing people know, bodies are flying left and right." Even so, USF&G still has plenty of challenges ahead. It is expected to post a \$53

million operating loss in 1991.

Despite the risks involved, some boards will go to considerable length to woo an outsider. At Allied-Signal Inc., where an unwieldy bureaucracy and a failed diversification effort had pounded earnings, CEO Edward L. Hennessy Jr. stepped down six months before his scheduled retirement to make room for Bossidy from GE. Allied's board was so eager to recruit an outsider that it quickly accepted Bossidy's demand that he be named CEO immediately, rather than serving time in a subsidiary role.

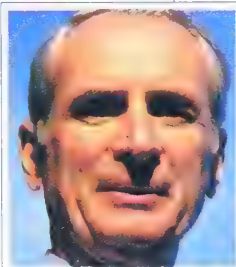
Boards often turn to an outsider because a dominant CEO has refused to groom an internal successor or has forced out any credible candidates. At Wang Laboratories Inc., founder An Wang and his eldest son Frederick held a tight control over decision-making, prompting other top executives to leave. Meantime, Wang's debt was soaring, and the company entered technical default on its loans in 1989. Finally, lenders insisted that the computer maker recruit a heavyweight from outside. Wang turned to Richard W. Miller, who had headed General Electric Co.'s consumer electronics unit, as its new chief.

CUTTING JOBS. Miller joined Wang in August, 1989, as president and COO, and assumed the CEO title seven months later, after An Wang died of cancer. Since then, he has sold off assets such as a switch unit and its computer-leasing business. Miller has also brought in a new executive team, recruited from Unisys, Digital Equipment, and Thomson Consumer Electronics. Unfortunately, there are no quick fixes at Wang. In June, Miller said that he will eliminate roughly 4,000 jobs, or 23% of Wang's 17,500 work force. And for its most recent year ending in June, the company lost \$385.5 million on sales of \$2.1 billion.

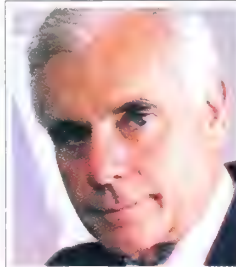
Nor has an outsider worked magic at Browning Ferris Industries Inc., which recruited former Environmental Protection Agency Chief William D. Ruckelshaus in 1988 to help spruce up its image. Ruckelshaus' lack of operating experience has hurt the garbage hauler and driven many senior officers out of the company. Though BFI's image among regulators has improved, profits have slipped and debt has soared. With troubles mounting, BFI President John E. Drury resigned in January, complaining that Ruckelshaus lacked a bottom-line approach to management. BFI's ex-chairman Harry J. Phillips Jr. recently returned from early retirement to help get BFI on track.

Will the trend toward outsiders continue once the economy is back in full swing? Most likely. With foreign competition heating up and the prospect for growth in the U.S. less than stellar, CEOs will remain under enormous pressure. And that means the odds will keep growing that a new face will show up in that plush corner office down the hall.

By Bruce Hager in New York, with Lisa Driscoll in New Haven, Joseph Weber in Philadelphia, Gary McWilliams in Boston, and bureau reports



MILLER: TRIMMING THE RANKS AT WANG



JOHNSON: HEATING UP CAMPBELL SOUP

COMMERCIAL SPACE

A SMALL STEP FOR MAN —A TINY ONE FOR INDUSTRY

Why the commercial space-launch business can't get airborne

High over the Pacific on July 17, a slim, white rocket called Pegasus dropped from under the wing of a B-52 bomber and shot upward on a plume of fire and smoke. But something was wrong. Minutes after takeoff, radar tracking stations couldn't pick up the stubby-winged Orbital Sciences Corp. rocket with its cargo of seven Pentagon satellites. Engineers at OSC, a commercial space company in Fairfax, Va., waited nervously until, hours later, the Air Force spotted the missing satellites. The birds were in a lower orbit than planned, cutting their anticipated lifetime from three years to one.

Pegasus' less-than-stellar performance is the latest in a string of woes for the fledgling commercial launch industry. On June 18, an Orbital Prospector rocket was destroyed after veering off course. Two months earlier, a General Dynamics Atlas carrying a \$50 million Japanese communications satellite crashed in the ocean. And last year, the European rocket Ariane and Martin Marietta Corp.'s Titan failed to deliver cargoes into orbit. Although the success rate of private launches is more than 90%, "a string of unrelated failures has cast a cloud over the future of the business," says Peter Nesgos, an industry dealmaker.

Now, there's one more thing to worry about: After a big buildup for what was billed as a bright future, too many rockets are chasing too few payloads. That has made some companies, such as Orbital, almost completely dependent on

Uncle Sam. And others are floundering in the search for customers. "Rocketry is a tough business," says Scott Pace, deputy director of the Commerce Dept.'s Office of Space Commerce.

That wasn't such a worry just two years ago. Then, the first non-government space launch in the U.S.—

And entrepreneurs had started sub companies as Orbital and American Rocket Co. in Camarillo, Calif.

Meanwhile, McDonnell Douglas, General Dynamics, and Martin Marietta stood ready to use their military boosters to launch big commercial payloads. It all had the government's blessing, especially because Uncle Sam had decided to stop lifting commercial satellites after the 1986 Challenger disaster. "It's very important to the industrial health and growth of the country to have a commercial launch industry," says the Commerce Dept.'s James Frelk, head of the Office of Space Commerce.

RARE BIRDS. But now, U.S. efforts to commercialize space resemble a blind hole rather than a shining star. Orbital factories are still distant dreams. And

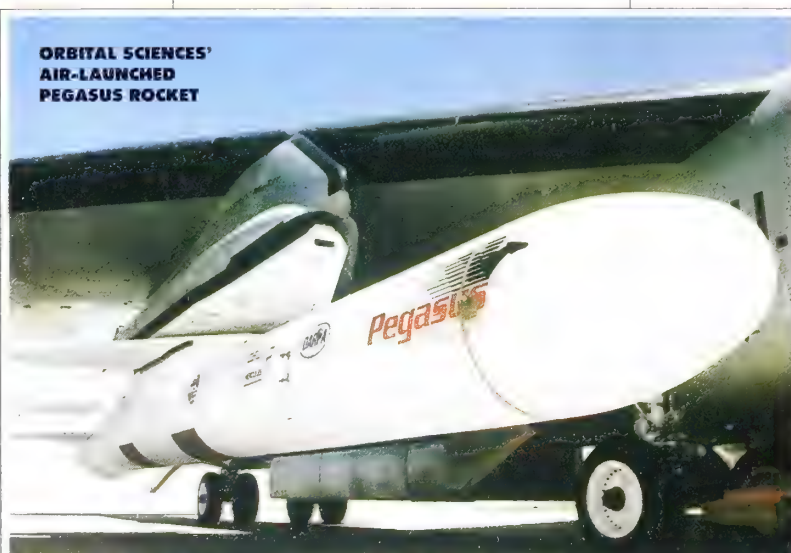
while Motorola Inc. and others plan to loft fleets of small satellites for communications or remote sensing, that may not happen this century.

So, "all of a sudden," says consultant M. R. Oderman, of CSP Associates in Cambridge, Mass., "there is a gross imbalance between supply and demand." At current production rates, there are enough of McDonnell Douglas Delta, GD's Atlas, Martin Marietta's Titan, Europe's Ariane family, and Chinese Long March rockets to lift 185 billion payloads a year.

The rocketeers are vying to loft huge communications satellites at \$50 million to \$100 million per launch for the U.S. and foreign governments. But analysts doubt yearly demand will exceed a dozen flights. That reflects competition from longer-lived satellites, fiber-optic cables, and the end of the backlog of satellites developed after the Challenger explosion.

Already, Martin Marietta has all but dropped out of the commercial space race, preferring to ship off its Titans for the Air Force. Other big companies aren't sanguine. "It's not a real rosy picture for us," says Bob Cowls, general manager of McDonnell Douglas Commercial Delta Inc.

In the scramble for business, U.S.

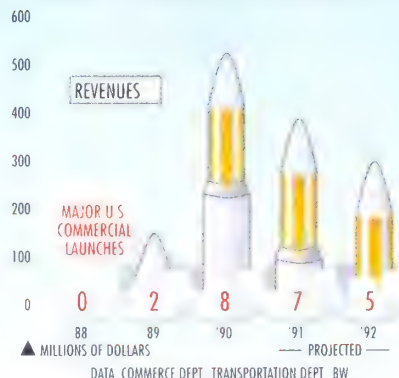


ORBITAL SCIENCES' AIR-LAUNCHED PEGASUS ROCKET

TOO MANY ROCKETS...

Company/U.S. commercial launchers	
MARTIN MARIETTA	Titan
MCDONNELL DOUGLAS	Delta
GENERAL DYNAMICS	Atlas
ORBITAL SCIENCES	Pegasus and others
TELER SYSTEMS	Conestoga and others
AMERICAN ROCKET	Aquila and others

...NOT ENOUGH PAYLOADS



of a British TV satellite aboard a McDonnell Douglas Corp. Delta rocket—was heralded as the birth of an industry. Experts had long predicted that orbiting factories would one day make drugs and other products in the weightless environment of space, where proteins, for example, form purer crystals than on earth.

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companies accuse the Europeans of playing foul by subsidizing launches. The Europeans counter that the huge U.S. government market—everything from spy satellites to planetary probes—closed to them. Everyone is livid over the Chinese, who have contracted to launch three satellites at bargain prices. To make matters worse, the Soviets are beginning to peddle their launchers.

POSEIDON VENTURE. What's more, in the U.S., hundreds of Poseidon missiles and other ICBMs are being decommissioned. Lockheed has a scheme to turn Poseidons into cheap commercial rockets, which could wipe out the small launcher companies. At a July 31 hearing, Congress began trying to sort out what to do about these ICBMs.

Despite the glut, most U.S. commercial rockets will likely remain in production—thanks to Washington. McDonnell Douglas can count on roughly \$300 million a year in federal business for about

**In the U.S., surplus
military rockets
may add to the glut of
launch vehicles**

six launches mostly of military payload. Martin Marietta is raking in \$7.3 billion from the Air Force for 41 Titan launches. And Orbital, which earned \$59.4 million on revenues of \$59.4 million in the first half of 1991, has grown from startup by collecting 95% of its revenue from Uncle Sam, mainly money from NASA, the Air Force, and the Defense Advanced Research Projects Agency.

Washington is still trying to jumpstart the business. Spinning off new industries and technologies has always been one justification for the space program, and NASA is helping fund launches by Orbital and EER Systems Corp. in Vienna, Va., of university experiments in crystal-growing and other microgravity research. With Pegasus, Orbital is also positioned to take advantage of the key lesson of the gulf war—the military's need to quickly launch tactical communications and spy satellites.

But that may not be a big enough foundation on which to build an industry. "We have to have real, nongovernment customers to take this beyond just a government bootstrap program," says NASA Deputy Administrator James Thompson Jr. So far, private companies aren't responding. That raises a painful question: Will the commercial launch business ever really blast off?

By John Carey with Seth Payne in Washington and Eric Schine in Los Angeles

Developments to Watch

EDITED BY OTIS PORT

CHEAP SOLAR POWER: IS THE DREAM COME TRUE?



Has an 80-year-old scientist in Athol, Mass., found the key to economical solar energy? Alvin M. Marks has patented a process that he claims is 80% efficient at converting sunlight into electricity. That's so much better than anything else around—as much as a fourfold increase—that many skeptics dismiss Marks out of hand. But not the

Electric Power Research Institute, the electric industry's research arm. EPRI is backing Marks with \$100,000. The idea stems from Marks' early, and underfunded, work Lumeloid—a thin, polarizing film covered with tiny molecular “antennas” that absorb sunlight and produce an electric current. Marks claims that a two-layer stack of his transparent material, with the layers oriented at right angles to each other, is so efficient that capital and production costs come to only 1¢ per kilowatt hour. That's about a fifth of current typical costs from fossil fuels. And other photovoltaic systems now in use are lucky to achieve 10% efficiency and costs of 25¢ per kilowatt hour. While Lumeloid's efficiency seems promising, skeptics warn that the material needs to prove itself in real-world, commercial installations.

HIS COLLAR HELPS KEEP FIDO'S TRAP SHUT

Four neighbors have a dog that doesn't like being left alone and barks incessantly whenever it is. And its owners don't want to be bothered with training the dog to bear its solitude in silence. If some peace and quiet are worth \$50, Canine Concepts Inc. in Austin, Tex., has just the gift for your neighbor: a “smart” dog collar that will train the pet not to make a nuisance of itself.

Working with Texas Instruments Inc., Canine Concepts has developed a microchip that can distinguish between the pattern of barks that a dog makes to sound an alarm—sharp, loud barking—and the yelps that signal loneliness or a fascination with the moon. When the Silencer collar detects the latter, it generates an ultrasonic noise that's unpleasant for the animal. When the nuisance barking stops, the collar turns off, too. The dog soon catches on, says Canine Concepts, yet the training won't affect the dog's performance as a guardian.

ARMORING UP EUROPE'S DEFENSE— ON-LINE SERVICES

In late July, the European Commission voted to push ahead with a special program to spur development of more on-line information services, especially data bases, by European companies. The move seems aimed squarely at blunting plans by foreign information providers, mainly U.S. suppliers, to increase their domination of Europe's on-line services. The drive kicked off in 1989, when the EC budgeted \$42

million for a two-year study dubbed Impact, for Information Market Policy Actions. The findings convinced EC ministers that aggressive action is needed just to preserve Europe's share of its own information markets. Now, the EC wants to spend nearly \$120 million over the next five years on Impact 2, helping to fund the creation of new on-line services. However, some member countries, including Germany, are calling for a smaller outlay, more in line with the original budget. So the full scope of Impact 2 remains uncertain.

A 'GREEN' HOTEL MAY BRING IN THE LONG GREEN

First, there were environment-friendly products such as laundry detergents that use no phosphates and pesticides that forgo petrochemicals for nature's own insect killers. Now, a Boston organization plans to bring the “green revolution” to notorious consumers of throwaway products, from sample toiletry bottles to cleaning supplies: hotels.

Saunders Hotels Co. is remaking its landmark Boston Park Plaza Hotel & Towers into an environmental showcase. Disposable utensils will be banned from the cafeteria. In offices and kitchens, paper, steel, and glass will be routinely recycled. And all 977 guest rooms are getting energy-efficient shower heads and double-glazed windows—plus bathroom dispensers to eliminate the annual need for 2 million plastic bottles of shampoo and lotion. The hotel's “greening” is already pulling in that other kind of green. Publicity about the new ecological approach has helped land two upcoming conventions.

TAKE A LASER, SOME POWDER— AND PRESTO! A 3-D MODEL

Today, getting products to market faster is crucial to success. That's why “desktop manufacturing” systems are galvanizing many companies. In just hours, such equipment can convert a computerized design into a real-life model that managers can touch and hold, cutting weeks from the time it usually takes to craft a model.



3-D Systems Inc. in Valencia, Calif., pioneered the technology in 1988. Its machine slices an electronic design into a stack of superthin layers. Then, a laser rebuilds the overall shape, slice by slice, in a vat of liquid plastic that hardens where the laser scans. More recently, a half-dozen other approaches have been developed by suppliers such as Cubital in Warren, Mich., DTM in Austin, Tex., and Light Sculpting in Milwaukee.

The latest technique is under development at Massachusetts Institute of Technology. A team headed by Emanuel Sachs, a professor of mechanical engineering, has built a prototype system that essentially prints the successive layers by combining elements of xerography and ink-jet printing. Instead of liquid plastic, the MIT system starts with a powder similar to the toner in copiers. Each slice gets “printed” by tiny glue jets that squirt a binder on the powder areas that should be fused. What's unique about this method is that the powder is a ceramic, so the process can also produce molds for casting a finished part in metal or plastics.

We've noticed recently that almost every computer manufacturer and software company is talking about one thing. Open systems.

Unfortunately, each of those companies has a different definition of open. To some it means UNIX®-based systems. To others it signifies compliance with standards. To many it merely suggests the ability to run off-the-shelf programs.

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HEALTH INSURANCE THAT ISN'T

Regulatory loopholes have let con artists bilk thousands of small businesses and their employees

To cut down on spiraling health-insurance costs, David Ouellette's employer switched from Blue Cross & Blue Shield of New Hampshire to a new plan set up specially for small businesses. Ouellette, who makes a modest salary as a lab manager at Chemtan Co., a leather tanner in Exeter, N.H., barely noticed the move to the new plan, which was offered by Boston-based Harbor Medical Administrators Inc. Then, in late 1989, his wife, Karen, had twins three months early. Doctors and nurses kept the fragile infants in incubators for weeks, monitoring them around the clock. They managed to save one. The cost: \$220,000.

After the Ouellettes brought the surviving baby home, they discovered that Harbor had paid none of the medical bills. Now, the hapless couple is trying to keep the hospital and doctors at bay while Chemtan sues individuals associated with Harbor, one of whom says it lacks the resources to pay the claims. And federal officials investigated the health plan, alleging that its executives milked its funds for their personal use. "I thought I had a safety net," says David Ouellette. "But when the net breaks, you go into a free fall, and there's nothing you can do."

Harbor is just one of a growing number of health-insurance providers that organize and act as administrators for groups of small companies such as Chemtan. Companies that participate in multi-employer welfare arrangements, or MEWAs, as they are called, generally self-insure by depositing premiums in a reserve fund overseen by the administrators. MEWAs, whose premiums are often 10% to 40% cheaper than coverage from established insurance companies, have caught on: There are at least 3,000 of them.

While good MEWAs fill an important need, too many are blatant rip offs. According to the Labor Dept., which over-

sees MEWAs, illicit plans have left \$300 million to \$500 million in unpaid claims, stranding thousands of people without insurance. Since the health plans generally aren't licensed by states, victims usually can't get reimbursements from state-run insurance-guaranty funds.

State and federal regulators, who for

Florida have set up teams to investigate the plans.

Rogue MEWAs often operate like classic Ponzi schemes (illustration). The plan administrators, who collect premiums and pay claims, set aside in reserve only a portion of the money. They pocket the rest, typically by paying themselves hefty fees, which they use to finance other businesses or support extravagant lifestyles.

After two or three years, accumulated claims usually begin to surpass the skimmed flow of premiums, the reserve fund becomes depleted, and the administrators stop paying claims. When employees with unpaid bills complain, administrators will sometimes try to pay claims or sell new policies. Or they simply shut down, leaving employees bereft.

What has attracted unscrupulous operators to MEWAs is the dearth of regulation. In 1982, Congress subjected them to certain kinds of state supervision, but the measure left plenty of room for the wily to maneuver. When state regulators crack down, for instance, MEWA operators can delay matters by going to court. Judges usually demand a Labor Dept. ruling on whether this is a state or federal matter, which can take months.

MOVING AROUND. Among the more egregious loopholes is that MEWA operators, unlike insurance companies, are not required to register or file any financial documents with most states. When things get hot in one state, they simply move to new hunting grounds, confident that regulators won't be able to track their movements and coordinate enforcement. Michigan is one of the few places with strong MEWA regulation—and not much of a problem.

The man behind the Harbor Medical mess, Richard Rowe, took advantage of the regulatory hodgepodge. For at least four years, he apparently profited from health plans in Boston and Atlanta that had clients in 16 states.

Finally, last year, Georgia regulators



Embezzler Rowe (upper right); White (bottom center) found out too late that her insurer was broke

years were oblivious to abuses, are finally starting to crack down. Since 1990, administrators of two of the largest health plans have been indicted on federal charges ranging from fraud to embezzlement. The Labor Dept.'s Inspector General's Office is conducting more than 30 major probes of MEWAs. Georgia and

zed his Atlanta health plan for unpaid ms. When a grand jury indicted him theft in that case, he fled to Denrk. Then the feds, who had gotten on case, extradited him. Four months , Rowe pleaded guilty in Boston fedl court to 22 criminal counts, includembezzlement, paying kickbacks, spiracy, and reporting violations. Intigtators say Rowe used funds from MEWAS, which covered more than employers, to fund other businesses l pay for boats, vacations, and other sonal items. His two insolvent Boston ns failed to pay more than \$4.3 milin claims. Rowe is awaiting sentenc. His lawyer didn't respond to rests for comment.

rafty health-plan operators often fle regulators by setting up phony erves. A federal grand jury in Orlan-is investigating International um of Florida Inc., which rida regulators took r in April, 1990, leav-\$16 million in unpaid ims. The takeover s delayed six months er IFF told regulators had new securities rth \$3 million in its re-ve. Investigators cond the capital injection ne from offshore companies l was arranged by insurance ultant Alan Teale, who is the sub- of a Senate subcommittee inquiry cerning the collapse of two other iners (BW—July 29). It turns out that never owned the securities, so they ldn't be sold to pay claims, officials . Florida Insurance Commissioner n Gallagher recently told a Senate aring that the IFF multicompany uth plan "was a pretense to make ney for its principals." Stanley M. Sil; attorney for IFF founder George V. herty, denies his client committed ud. Silver says Doherty "paid \$75,000 securities he believes could be liquied and cashed." Teale's lawyer, Miel Weinstock, says Teale didn't arge the IFF securities deal.

Among those left in the lurch were 70 ployees of South Dade Electrical Sup- Inc., which signed up with IFF 1988, when its longtime in-er announced a 40% e hike. South Dade, ich paid \$290,000 in emiums, now has 0,000 in unpaid claims l must pay \$100,000 the state insurance l to compensate MEWA tims. Says President n Elliott: "This is the rst nightmare in my 25 ars in business."

Sometimes, shady MEWA operators will

HOW THE SCAM WORKS



Insurer siphons off premiums by paying itself hefty fees instead of building up reserves

Insurer shuts down, leaving employees with huge unreimbursed medical bills

DATA: BW

lull buyers with claims that their health plan is guaranteed by a reputable-sounding insurance company. That's what Brenda White, a secretary for Forsyth Vault & Seal Co. in Cumming, Ga., says happened to her. She thought her plan, Dimensional Health Insurance Trust, was solid because American Equitable Life Insurance Co. in Dallas backed it. "I wish I had paid more attention," she says. The day after her November, 1989, car accident, she learned that Texas regulators had seized American Equitable for insufficient reserves and non-payment of claims.

GUILTY PLEAS. Stuck with a \$30,000 medical tab, White is suing Dimensional administrator Arden O. French and others for fraud. French replies that her suit is nonsense and says he had no way of knowing about problems at American Equitable, where he switched after Dimensional's previous insurer announced a rate hike. "I've been in the insurance business 23 years, and I've never been sued before," he says. American Equitable executives could not be located.

Some bogus MEWAS flaunt tenuous or nonexistent links with well-known insurers. The lawnmower-parts distributor that employs Mark Frank through an employee-leasing outfit called Cap Staffing Inc. was lured by the Travelers Insurance Co. umbrella logo and name on written material for the Cap-owned MEWA.

Eventually, insurer is unable to pay claims from the depleted flow of premium dollars

Trouble was, the only dealings Charlotte-based Cap Staffing had with Travelers were that it used the insurance giant to process claims. Three Cap Staffing principals recently pleaded guilty to 27 counts, including mail fraud, embezzlement, and conspiracy; three others, who pleaded innocent, await trail.

Meanwhile, Frank, a salesman who earns \$30,000 a year, has \$260,000 in medical bills for his leukemia-stricken daughter Susan's bone-marrow transplant. "I'm facing bankruptcy and financial ruin if these bills aren't paid," he told a Senate subcommittee last year.

Others who paid premiums to health-plan bunkum artists share his heartache. Nothing equals the shock of a horrendous medical bill. "I used to take insurance for granted," says Ouelette. Now, the sudden lack of it threatens to take him to the poorhouse.

By Walecia Konrad in Atlanta, with Gail DeGeorge in Miami and Susan B. Garland in Washington

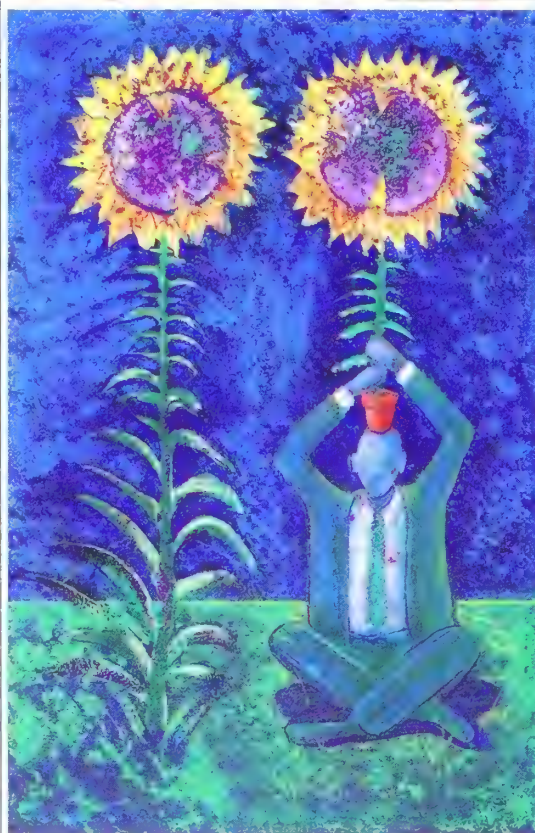
SPOTTING GROWTH STOCKS THAT WON'T POOP OUT

The key is fast-rising revenues combined with juicy margins

All eyes are on growth stocks, and investors are keeping their fingers crossed that Liz Claiborne isn't lurking inside their portfolios. It's not the dress designer they fear, but what happened on July 22. The apparel maker reported second-quarter earnings in line with analysts' forecasts. But management also said second-half sales and earnings would not match the gains of the first, and investors who bought the company as a growth stock headed for the exits. Shares plunged \$7.25, or 15%, on that one day.

Analyst Robert W. Gay of Donaldson, Lufkin & Jenrette Inc. wasn't surprised. He had spotted the slowdown in sales and noted that profit margins were under pressure, so he put the stock on his sell list just days before. Gay is no expert on the apparel industry. He's a quantitative analyst who applies computers to a universe of growth stocks to determine which can maintain robust profits and which will poop out.

That's a critical question nowadays as the Dow Jones industrial average girds up for another attempt at a new high. With the economy still sluggish, no one's counting on big earnings from the cyclical stocks. So if the market's going to



make new ground this year, it will do it on the strength of growth stocks.

But all growth stocks—companies whose profits grow faster than those for the market as a whole—eventually slow down and lose their premium stock mar-

ket valuation. Some of the tried-and-true growth stocks of recent years—Disney, McDonald's, and MCI Communication—seem to have lost their earnings momentum. Others, including Coca-Cola, Microsoft, and Philip Morris, are still on track. Until recently, Liz Claiborne looked like a steady, reliable growth company, but now that's in question.

Growth-stock investors are hardly of a single mind. For instance, Herb Hutzler, who has been running the Weingarten Fund for more than 20 years, is sticking with Liz. Says Hutzler, "This earnings slowdown is temporary."

'FANTASY LAND?' The key to successful growth-stock investing is the ability to sense when the profit wave has run its course and when it's taking a rest. Gay takes a purely quantitative approach to making that judgment. Most Wall Street analysts say that's impossible to do without qualitative fundamental analysis, such as quizzing the management about new products. Says money manager Roger Engemann of the firm that bears his name: "You have to judge whether the CEO is in fantasy land, or he has his feet on the ground."

Some investors look to valuation measurements such as price-earnings ratios or price-to-book value ratios, which can be misleading. Consider U.S. Surgical, one of the hottest stocks of the past few years. It sells for an apparently outrageous 63 times earnings, yet its products have so much potential that the high valuation could well be warranted (see "When you're a growth-stock investor, you're always dealing with high-priced stocks," says Gay. "What does count is the direction and level of the company's sales-growth rate.")

Most growth investors would agree that nothing works better for a growth stock's earnings than good old-fashioned sales growth: building more and better products and selling more of them. In theory, a company that is skilled at increasing the top line is the top dog.

NOT ALL GROWTH STOCKS ARE ALIKE

EARNINGS ACCELERATING			STEADY EARNINGS GROWTH			EARNINGS DECELERATING		
Stock	Price	P-E ratio	Stock	Price	P-E ratio	Stock	Price	P-E ratio
ADC TELECOMMUNICATIONS	28¼	15	AUTODESK	54¾	23	ABBOTT LABORATORIES	53¾	23
ADOBE SYSTEMS	53½	25	COCA-COLA	60¼	27	ALBERTSON'S	38½	2
ALDUS	40½	22	COSTCO WHOLESALE	44¼	44	FEDERAL NAT'L MORTGAGE	57¾	15
GAP	34¾	30	HOME DEPOT	48½	51	GILLETTE	38¾	23
LINEAR TECHNOLOGY	24¼	25	MICROSOFT	73½	30	JOHNSON & JOHNSON	91½	23
MEDCHEM PRODUCTS	13¼	16	NIKE (CL. B)	43½	12	LIZ CLAIBORNE	43½	17
NICHOLS RESEARCH	11	12	NOVELL	58¾	33	MERCK	128¾	26
PRICE	54½	21	PHILIP MORRIS	67¾	16	PEPSICO	31¾	21
UNIFI	39¾	20	U.S. SURGICAL	73¾	63	WAL-MART STORES	47¾	40

DATA: DONALDSON LUFKIN & JENRETTE SECURITIES CORP., BRIDGE INFORMATION SYSTEMS

but a lot happens between the top and bottom lines that can affect earnings. Points to Abbott Laboratories, where earnings have increased 17% a year over the last five years, but sales have grown at only a 13% clip. What accounts for the difference? Abbott has been able to boost its profit margins.

ADBLOCKS. There's nothing wrong with fatter margins. "Margin improvements can go on for a long, long time," says Hutzler. "I consider margin growth more important than sales growth in selling stocks." Profit margins can be boosted in a number of ways: reducing overhead, improving inventory controls, raising prices. But there are limits to raising margins. For one thing, companies may be unable to raise prices in an industry where demand is waning. In computers, for example, profit margins are shrinking because of intense competition and falling prices.

Corporate earnings have grown in other ways that may not be sustainable. In the late 1980s, many companies bettered their bottom lines because tax rates dropped. That was great, but it came in the form of an act of Congress, not managerial skill. Stock buybacks that increased financial leverage also boosted per-share earnings for several years by spreading earnings over a reduced number of shares. But the wave of share buybacks probably over; if anything, the trend toward issuing—not retiring—equity. There's no question that the growth stocks most likely to please investors are those with accelerating sales growth and rising profit margins. That powerful combo will allow companies to capture a larger proportion of an increasing number of dollars. Among those that Gay highlights: software producer Aldus, retailers The Gap and Price Co., and text processor Unifi.

Right now, such stocks are few and far between. The next best picks: those with rising sales growth and steady margins, or sustainable-growth stocks, such as Autodesk, Coca-Cola, Costco Wholesale, Home Depot, and Novell.

Investing has turned bearish on some of the most successful growth stocks of the past decade, such as Merck. As the world's leading drug company, Merck is selling, he argues, because sales growth is turning down, and the gross margin, which expanded by about 25% over the last five years, is topping out. To him, the stock isn't worth 26 times earnings. That's definitely a minority view on the part of a drugmaker, as its earnings growth and stock price so far reveal no such problems. Yet even the best of growth companies eventually lose momentum. In growth-stock investing, the game is not only to know when to get on the bandwagon but to jump off before it stops.

By Jeffrey M. Laderman in New York

U.S. SURGICAL HAS HEARTS BEATING FASTER

Last fall, Massachusetts Financial Services Co. sold its \$10 million stake in United States Surgical Corp. After all, the mutual-fund company had more than doubled its money in less than a year, and the stock looked fully priced. A few months later, Mark J. Cunneen, who analyzes health care stocks at Mass Financial, spent some time with the company's management getting briefed on U.S. Surgical's new products. He quickly realized the stock had been sold too soon. "The company has tremendous opportunities," says Cunneen. His fund went back into the stock and now owns 125,000 shares.

Massachusetts Financial is not the only institution that has returned to U.S. Surgical—and the stock price shows it (chart). This year alone, the stock has doubled, and over the past 2½ years, it has jumped ninefold. Investors have been panting for health care companies, and U.S. Surgical is one of the hottest in the hottest stock group. Portfolio managers and analysts are singing hymns of praise to this Norwalk (Conn.) manufacturer of surgical supplies.

"I love the company," says Warren B. Lamert, an analyst for the Janus Group of Mutual Funds. Janus sold its shares in the first quarter but has revised its earnings forecast twice and bought back the stock. Says Charles A. Mangum, portfolio manager of the Fidelity Select Medical Delivery Fund: "It's in the right field, doing the right things."

FUTURE TECH. What's got investors gaga over this company is its commanding position in producing laparoscopic instruments. These tools allow surgeons to perform operations through tiny punctures rather than through large open incisions. Such procedures can cut the recovery period from gall bladder surgery, for example, from about six weeks to only a few days. Now, laparoscopy is used mainly for gall bladder removals, appendectomies, and gynecological procedures. But analysts think that by the end of the decade, 80% of abdominal surgery will employ the technique.

Right now, only 20% of U.S. Surgical's \$514 million in annual sales comes from laparoscopy. But analysts say laparoscopy alone could bring \$1 billion a

year in sales by 1994. In the first half of 1991, the company's total sales jumped 75%, and earnings 78%, vs. the first half of 1990.

STRATOSPHERIC. The question for investors is whether the growth explosion is big enough to justify U.S. Surgical's stock price. The stock sells at 63 times the past 12 months' earnings, nearly four times the price-earnings ratio of the Standard & Poor's 500-stock index. Based on earnings projections of brokerage house analysts, the stock is selling at about 38 times 1992 earnings. The company also sells at a stratospheric 14.7 times book value vs. about twice book for the market as a whole. Still, some see the laparoscopy market as potentially so huge that those traditional yardsticks are meaningless. Says Kurt H. Kruger, a health care analyst for Hambrecht & Quist Inc.: "This is a cheap stock masquerading as an expensive stock."

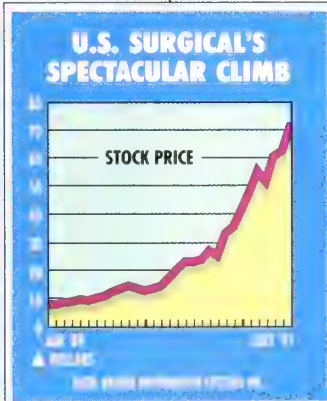
Perhaps so. Although the company may be first in laparoscopy, it's not the only player around. The Ethicon Inc. division of Johnson & Johnson, which competes with U.S. Surgical in the surgical staple market, plans to introduce about 40 laparoscopic products this year—and it plans to market them by doubling its sales force to

350 by yearend. That kind of competition is bound to curb some of U.S. Surgical's stupendous sales growth. Indeed, company officials are trying to dampen investor expectations. Warns Marianne Scipione, a U.S. Surgical vice-president: "To duplicate the past is impossible."

Analysts tracked by Zacks Investment Research forecast a five-year annual earnings growth rate of 31%. Some shareholders say that's far too low. "Laparoscopy is revolutionary," says G. Kenneth Heebner of Capital Growth Management. "This market will be bigger than most realize. This stock can become a religious experience for its owners."

Heebner may be right. If U.S. Surgical meets or exceeds the high expectations, shareholders will be floating on air. But if profits fall short, the stock could drop so far so fast that investors will hit the ground—and hard.

By Lisa Driscoll in New Haven, Conn.



DANCES WITH DEBTS: WHY ORION IS REELING

Rosy projections led to huge write-downs and angry bondholders

Hollywood has always loved a good mystery. One of the most intriguing these days involves Orion Pictures Corp.: Why is it on the brink of bankruptcy even though it's responsible for two of the biggest recent hits, *Dances with Wolves* and *The Silence of the Lambs*?

Orion began life nearly a decade ago as a tiny film company organized by former United Artists Corp. executives eager to create their own major studio. Perhaps its most notable achievement, however, has been a \$511 million mountain of debt. Orion executives are now busy negotiating with restive bondholders. The company, which has lost \$87.8 million over the past five quarters, missed a recent \$1.2 million interest payment to bondholders. Unable to tap its bank lines any further, Orion acknowledges that it could miss an additional \$56.9 million in scheduled interest and principal payments due by the end of August.

Why didn't *Wolves* and *Lambs* forestall this turn of events? The short answer: Orion's handful of hits, such as *Platoon*, *Bull Durham*, and *RoboCop*, were overwhelmed by its numerous dogs. Another explanation is more complicated. Orion has frequently used aggressive, and perfectly legal, accounting tactics to boost its reported earnings. That has helped the company raise roughly \$800 million in debt and equity to fuel its expansion.

BUYING TIME. Orion's chief tactic involves the way it accounts for production costs. All movie companies capitalize these costs, adding them to the balance sheet as assets instead of subtracting them from revenues. But they are supposed to write down the amount on the balance sheet at regular intervals and subtract the number from earnings if the box-office outlook for the films deteriorates.

Orion, though, always seemed to expect hits. "Some studios are definitely more optimistic than others, and Orion was al-

ways among the most optimistic," says David W. Free, a partner in the Los Angeles accounting firm Singer, Lewak, Greenbaum & Goldstein. Orion would delay, sometimes for years, taking write-downs on films that didn't measure up. It seemed to be buying time: pushing write-downs into the future with the vague hope that a string of smash hits would rescue it from its growing debt load. Orion had no comment.

When Orion eventually did adjust its optimistic projections to reality, the write-downs were prodigious: one-half the company's \$31.8 million loss in 1986 came from writing down 30 films it had

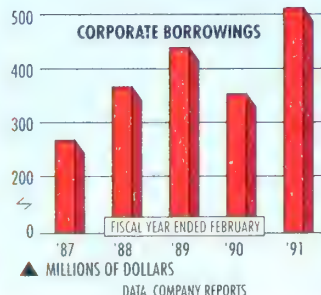


A STRING OF 1990 FLOPS...

Movie	Box-office receipts Millions of dollars
STATE OF GRACE	\$1.9
THE LAST OF THE FINEST	1.5
LOVE AT LARGE	1.4
EVERYBODY WINS	1.3
THE HOT SPOT	1.3

DATA: ENTERTAINMENT DATA INC

...SENT ORION'S DEBT BACK UP



released since 1982. In its most recent fiscal year, when it lost nearly \$63 million, more than half the \$32.8 million write-down came from films released during prior years. "Surprises like that really shouldn't happen," says Shadi Sanbar, director of Arthur Andersen Co.'s entertainment industry services unit.

Another surprise was Orion's belated disclosure this spring that the \$15.1 million profit it reported for the fiscal year ending February, 1990, was made possible by booking part of a \$175 million advance, received close to the fiscal year's end, from Columbia Pictures Entertainment Inc. for various rights in Orion's film and TV properties.

MISSED CHANCES. In recent weeks, Orion has been hit by a spate of shareholder lawsuits alleging that the company failed to disclose material facts about its worsening conditions. Chief Executive William Bernstein, who took control from 81-year-old founding Chairman Arthur B. Krim last spring, says the company's accounting practices are proper. But even Bernstein doesn't deny that the company had a string of stinkers in 1989 and 1990 (chart).

Just as dismal was the performance of Orion's TV production unit. It has produced almost no winners, subsisting mainly on revenues from *Cagney & Lacey* reruns. In 1991's first quarter, Orion closed its TV production unit, taking a \$18.4 million write-down. The company has been getting rid of other assets, selling many of the videocassette or broadcast rights to its past hits. Billionaire John Kluge, who owns 68% of the company, funneled \$23 million into Orion in return for a piece of the film *Mermaid*.

Orion's debt has caused it to miss some lucrative opportunities. In some cases, it was forced to cut back on equity investments in films and settle for simple distribution fees. For instance, it didn't acquire the foreign rights to *Dances with Wolves*, which Entertainment Data Inc. Vice-President Phil Garfinkle estimates grossed \$50 million overseas.

Orion executives and representatives of the company's bondholders are currently meeting in Orion's West Coast headquarters in Century City to negotiate the company's fate. Both sides say they hope to keep the company alive. Considering Orion's deteriorated balance sheet, that would truly be an Oscar-worthy performance.

By Ronald Grover in Los Angeles

GENE G. MARCIAL

THE COLD SHOULDER MAY HAVE MADE HANSON A HOT BUY

Shares of Hanson, the acquisitive British holding company, have been under heavy pressure since the company's mid-May announcement that it had bought a 2.8% stake in Britain's huge Imperial Chemical Industries. Many of Hanson's major British shareholders bailed out, switching their money into ICI, which they assumed was a takeover target. Hanson tumbled from \$23 per ADR (American Depositary Receipt) to \$16. But in recent days, the stock has rallied, edging up to \$18 a share as some American pros have taken the opposite route, placing heavy bets on Hanson.

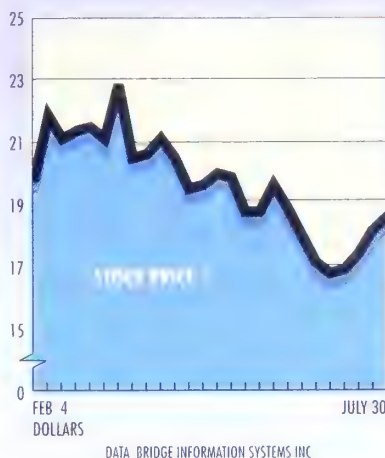
What's behind this new faith? F. Harry Nelson, an analyst at Louis Nix & Associates, says the decline in Hanson's shares "creates an excellent buying opportunity at the very time when the possibility of a successful bid by ICI enhances the company's earnings-growth potential while entailing virtually no risk." Hanson currently owns a string of industrial and consumer-product companies, including British Ever Ready and Imperial Tobacco in Britain and Jacuzzi, Kaiser Cement, and Peabody Coal in the U.S.

So far, ICI has rejected Hanson's merger overtures. No matter, says investment manager Charlie Rose, who has been a big buyer of Hanson shares recently. "Hanson is in a no-lose situation when it comes to ICI," he says. "With all that has happened, it has turned into a low-risk, high-return stock with the potential of hitting \$25 to \$30 a share" in 6 to 12 months.

LOOK FOR ASSETS? Rose, who runs C.J. Rose hedge fund, thinks some of ICI's operations, including pharmaceuticals and petrochemicals, would be a boon to Hanson. But even without a merger, he says, "Hanson will extract a big bucks or some assets from ICI." Rose believes Hanson may sell its stake to ICI at a hefty premium—something like greenmail—or settle for ICI assets, such as its pharmaceutical business, in exchange for stock.

Rose is also convinced that Hanson will make a major acquisition soon even if it doesn't acquire ICI, mainly to accelerate its sluggish earnings growth. This year, profits are expected only match last year's \$1.62 a share

HANSON IS SNAPPING BACK



because of the recession in Britain and the U.S. The absence of a major acquisition also contributed to slower growth. But in 1992, earnings are expected to edge up to \$1.85 to \$2 a share. What's more, Hanson, which has been a seller of assets this year, has built up a cash hoard of \$13 billion.

BUYOUT RUMBLINGS AT CRYSTAL BRANDS

Some investors in apparel maker Crystal Brands are getting mighty impatient with its stock, which hasn't budged—even after restructuring plans were announced on July 1. The upshot: It may not be long before Crystal's big holders band together and join a group rumored to be interested in launching a takeover bid.

One of the big investors who may participate owns a huge stake in a major department-store chain. If a buyout group is formed, expect a flurry of buying in Crystal shares, currently trading on the Big Board at 23. That's well below its high of nearly 38 and not much above the initial offering of 22 in 1985, when Crystal was spun out of General Mills. "The stock is worth at least 50% more than its current price," says one New York portfolio manager.

Crystal's announcement that it plans to sell unprofitable businesses and close some facilities didn't stir much interest in the stock. Chairman and CEO Richard Kral says he's confident that the planned changes will cut costs, pay down debt, and improve earnings. Not enough, says one stakeholder who has been asked to form a buyout group. "Cost-cutting and shutting fac-

tories are steps in the right direction," he says, "but they address only part of the problem." He argues that profit levels should be raised through increased sales, adding that management needs to focus more on that and also try to get the value out of some assets.

He notes that Crystal's jewelry business alone, which includes Monet, a leading maker of costume jewelry, is worth about \$23 a share. Crystal's apparel products also have well-known labels, such as Izod Lacoste, Evan-Picone, and John Weitz.

TRINKETS THAT COULD TAKE OFF

Many of the market's fallen angels in the 1980s have already staged a comeback, thanks to the market's continued advance. But not Russ Berrie, which traded as high as \$45 a share in 1987. It seems to be stuck at \$13, this year's low. However, some big value-oriented pros have turned bullish on the Big Board stock.

A leading maker of impulse gift items, such as stuffed animals, dolls, and coffee mugs, Russ Berrie "is very much an undervalued gem," says Ron Breitweiser of Clairvest. With the recession over, Breitweiser thinks an earnings turnaround is imminent. He sees sales of \$300 million in 1992, up from an estimated \$260 million this year, vs. 1990's \$245 million, with earnings rising to \$1.80 to \$2 next year from about \$1.30 to \$1.50 this year, compared with 1990's \$1.16. He figures the stock will go for twice its current price in a year.

Russ Berrie is the kind of company value players love. It trades near its book value of \$13 a share—a rarity among companies that historically generate a 20% return on equity. And its balance sheet is "superclean," with little debt. Plus, it's flush with working capital of \$154 million and cash of \$46 million, or \$3 a share, says Breitweiser.

One market that's expected to boost earnings: the nation's high schools. The company is increasing its participation in school fund-raising projects, where Russ Berrie's gift items, including back-to-school products, have become hot stuff, says Breitweiser. He figures that school orders will boost sales by \$85 million to \$100 million by 1993. Another big market: personalized coffee mugs imprinted with business logos or pictures of customers. These popular products are expected to add some \$80 million to sales in 1993.

PCs: WHAT THE FUTURE HOLDS

THE INDUSTRY IS IN TURMOIL. WHOSE TECHNOLOGY WILL DOMINATE THE '90s?

It was the end of an era. On July 3, after weeks of rumor and speculation, IBM Corp. and Apple Computer Inc. matter-of-factly announced a plan to team up in the personal-computer business. Apple and IBM? To industry insiders, it was a little like Jesse Helms and Jesse Jackson announcing that they were on the same ticket.

Concluded just a month before the

10th birthday of IBM's first PC, the sudden *glasnost* between the world's No. 1 and No. 2 personal-computer makers serves as a neat end point to the first stage of personal computing. Throughout that era, Big Blue and Apple were almost always on opposite sides. From its inception in Steve Jobs's garage, Apple was the quintessential Silicon Valley upstart. Youthful and self-consciously ir-

reverent, the company announced its audacious mission was to liberate computing power from the mainstream Establishment that had kept the most expanding technology locked up in air-conditioned glass rooms. IBM, of course, was the Establishment—East Coast, buttoned-down, and tradition-bound.

That IBM and Apple are now embracing says a lot about how the PC business



1 9 8 2

►Compaq Computer is founded by Rod Canion and other Texas Instruments engineers. Compaq starts with a portable clone of the IBM PC and goes on to become IBM's biggest challenger in the corporate market



1 9 8 3

►Lotus Development, led by Mitch Kapor, releases 1-2-3. The spreadsheet, which cost \$340,000 to develop, quickly becomes the best-selling program for the PC
►IBM aims at the school and home-computer markets with the ill-fated PCjr



1 9 8 1

►Four years after the first personal computers hit the market, IBM jumps into the IBM PC, which it promotes with Charlie Chaplin's little tramp

1 9 8 4

►Apple unveils the Macintosh, which Apple co-founder Steve Jobs calls an "insanely great" computer. Advertised as "the computer for the rest of us," Mac's easy-to-use graphics format sets it apart from the PC
►IBM releases the PC AT, an important upgrade to the original PC that remains the standard for PC cloning



1 9 8

►With Mac sales soaring, Apple's Jobs is ousted from the company by John Sculley
►IBM shifts Don Estridge, the executive



credited with launching the PC, into a corporate role. Lowe, who had originated the project, returns to the corporate mainstream
►IBM kills the PCjr

A SUCCESS STORY: THE IBM PC'S FIRST DECADE

\$8.5
1981

\$3.9
1981

anging and something about how erate both companies are to hold on their positions in Round Two. In the s, leading in PCs means leading in puters. Period. In their myriad is—from \$500 clones to \$2,000 lap- and \$25,000 network hubs—PCs al- y dominate the computer industry. i annual worldwide sales of about illion (chart), PCs now dwarf all oth- omputer markets. Mainframes, for ple, bring in only \$50 billion annual- ncluding sales of software, disk s, and other peripherals.

IER HORSEPOWER. In the coming de- , PCs will do far more. Chipmakers here's no reason they can't continue ouble microprocessor power every years, as they have done throughout 1980s. That will make possible desk- computers by the late 1990s with er surpassing today's supercom- rs. And, industry executives prom- that means there will be no letup in novation. "We have been racing to

get to the starting line," says John Scul- ley, Apple's chairman. "The really inter- esting stuff begins in the 1990s."

What's in store? For one thing, PC technology will be everywhere—in desk- tops, laptops, palmtops, and, the pundits say, in all sorts of consumer items. As the cost of microprocessors and com- puter memory drops—and as break- throughs in speech-recognition software occur—the amenities TV writers in the 1960s dreamed up for the fanciful Jetson home may become a reality. Imagine all sorts of appliances that know when to turn themselves on and off, toasters that respond to a spoken command, or phones that automatically search electronic Yellow Pages for a pizza parlor—then place your order.

In the living room, PCs, high-def-

inition televisions, stereos, VCRs, and la- ser disks will converge in a new multi- media information and entertain- ment system (page 62). "I see no reason that all those can't be part of one package," says Scott McNealy, chief executive officer of workstation maker Sun Microsystems

\$93.3
1991 EST.



1 9 9 1

► In a deal that could broadly alter the personal-computer industry, IBM and Apple agree to work together on technology. Chairmen John Akers and Sculley hope the deal revives profits



1 9 8 9

► Multimedia applications, such as ABC's '88 Vote program, start making their way to market. Microsoft Chairman Bill Gates predicts that multimedia—the integration of video, sound, and text—will be "bigger than everything we do today"



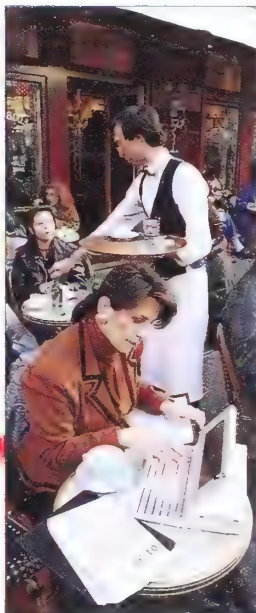
\$37.1
1991 EST.

WORLDWIDE
AL COMPUTER SALES
IONS OF DOLLARS

1 9 8 7

► IBM replaces the original PCs with the PS/2 line. Most PS/2s use Micro Channel, a proprietary format aimed at slowing down the clones

► Microsoft and IBM announce OS/2, which includes a Mac-like graphics format. They say it will replace MS-DOS, the original PC operating system



1 9 8 8

► Sales of IBM-compatible laptops begin to climb. A new species of smaller, "notebook" PCs, led by NEC's 4.4-pound UltraLite, appears



1 9 9 0

► The 10-year partnership between IBM and Microsoft begins to disintegrate after Microsoft's Gates promotes his Windows 3.0 graphics software at the expense of OS/2

U.S.
PERSONAL
COMPUTER
SALES
IN BILLIONS
OF DOLLARS



9 8 6

beats IBM to h the first computer l's speedy 80386

gs out its first mputer, the PC e. It's not a hit, but aptop clone is



PEOPLE ARE TALKING . . .



GEORGE BUSH
PRESIDENT

"I have a wonderful time
on personal computers. She [Michelle
Michelle] wears her hair as a PC.
Adults are never too old to learn.
Some people tell me the market for
PCs is diminishing, but that's hard to
believe when I'm just discovering
how valuable they are. There must
be a lot of people like me."



WILLIAM H. GATES III
FOUNDER AND CEO, MICROSOFT

"If the microprocessor hadn't come
along, I'd probably have become a
professor, which is certainly
different from what I do now."



ROBERT METCALFE
INVENTOR, ETHERNET NETWORKING
TECHNOLOGY

"The PC has made me rich."

Cover Story

Inc. Personal computers with user-friendly software will even make it possible for adults to program the VCR—or to send and receive facsimiles and download stock quotes into a personal-finance program that calculates the value of the family portfolio. And PCs will entertain and educate the kids—but not with today's simplistic, two-dimensional video games. Entertainment on these super-PCs will include programs such as interactive fiction, in which the player assumes the identity of one of the characters in a novel, chooses plot twists, then watches the action unfold on the screen. Nightly homework may involve tapping into remote data bases of text, video, and audio information, then filing completed assignments electronically.

And PCs will go wherever we do. The current boom in laptop and notebook PCs will continue as battery-powered machines take on all the powers of desktop models, including the ability to display color graphics. The next hot development, just under way, will be "pentop" machines that understand handwriting. By the end of 1991, IBM, NCR, Tandy's Grid Systems subsidiary, and a clutch of startups are all expected to be selling the tablet-size machines. Researcher BIS Strategic Decisions predicts that in 1995, when tablet computers have been refined, sales will hit \$1.5 billion.

'PERVERSIVE AS PHONES.' By mid-decade, a new breed of midget PCs is likely, too. Today's shirt-pocket-size computers will be updated to understand spoken commands. They'll talk back, too, reminding you of your spouse's birthday, for instance.

"In 10 years, PCs will become as pervasive as phones are today, and in sizes and shapes we can't envision now," says Richard D. Sanford, chairman of the 1,058-store Intelligent Electronics Inc. computer retail chain. "Everyone will have one. It is going to change the face of our very society."

At the office, desktop machines will become enormously powerful—and far easier to use. Much of the computer's processing power will be devoted to making interactions between humans and computers relatively painless. Handwriting will be an alternative to the keyboard. And instead of learning a series of computer commands to calculate the effect of a 1%

drop in the prime rate, you may be able to simply tell the computer to do work. Its voice-recognition software interpret your words and its expert-system programming will manipulate other programs needed to get the done. Business communications will jazzed up with a multimedia mix of dio, graphics, video, and text. Videoferencing will become commonplace.

BRAND X. All this and more is possible even likely. But before it happens, the PC industry has to reinvent itself. The glue that has held the business together for the last 10 years—the standard IBM laid down with the introduction of its first PC—is coming unstuck. From the minute it was introduced on Aug. 12, 1981, the \$1,565 IBM Personal Computer established the rules of the game. Following IBM's lead, clonemakers made PC standard ubiquitous from Texas Instruments to Timbuktu. Apple succeeded—starting with its Lisa in 1983, and then with the Macintosh in 1984—by defining itself as the alternative to the IBM standard.

Now, the industry needs a new model. To read handwriting, understand the human voice, manage digitized images and sounds—and take on the big computer jobs that mainframes and minicomputers still do—tomorrow's PCs need a more up-to-date foundation. Neither the IBM standard nor the more user-friendly Apple Macintosh design are really up to the task. That's why, together, Apple and IBM are looking to develop a new design that, in the mid-to-late-1990s, can neatly supplant the original IBM standard as well as Apple's current design. Their agreement, if it pans out, will produce new computers using powerful RISC (reduced instruction-set computing) chips and a radically new form of operating-system software.

And this time around, IBM wants to make more than put a Big Blue imprint on the next generation of PCs. By making

technology more proprietary, IBM wants to shake the pack of clonemakers that has plagued it in the first PC era. "At the end of 10 years, IBM is no longer happy with the rules," says William H. Gates III, chairman of software powerhouse Microsoft Corp. "They created something they can't live with."

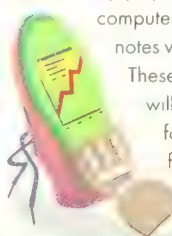
Clones were the unintended outcome when IBM Chairman John R. Opel approved

GO-ANYWHERE COMPUTERS

Love the idea of an electronic Filofax, but intimidated by today's 'personal organizers'? New, ultra-compact PCs may be what you're waiting for. They will let you update phone numbers and calendar entries simply by speaking to the

computer, or jotting down notes with a special pen.

These handy machines will also come with a fold-up keyboard for on-the-fly word processing

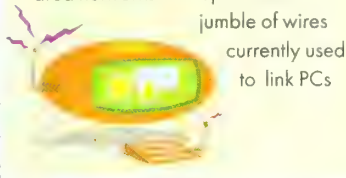


SNAPPING THE WIRE TETHER

NEW
PC
IMPROVING

Hate having to hunt for a phone jack every time you send or receive data by laptop computer? By the mid-1990s, you won't have to.

Technologies that connect PCs into wireless phone networks will get more reliable. Laptops will even bounce signals off satellites. In the office, wireless versions of local-area networks will replace the



jumble of wires
currently used
to link PCs

ash program to into personal com-
rs. He dispatched
m of 13 engineers
oca Raton, Fla., to
e up with a com-
r that could halt
advance of compa-
such as Apple,
modore, and Tan-
Starting in 1977,
e companies had
n the personal-
puter concept—
eered by techie
epreneurs who
microcomputer
to hobbyists—and
n making a real business out of it.

IMAKER. Opel was particularly
ned by the stunning progress of Ap-
By 1980, Steve Jobs's startup had
n to a \$117 million company. And
e's rainbow logos were beginning to
up in the big corporations where Big
's mainframes ruled.

ed by longtime IBM executive William
owe, the team at Boca Raton was
n one year to come up with an an-
to the Apple II. To meet the dead-
on their "Acorn" project, they broke
IBM rules. Don Estridge, who took
when Lowe was shifted to another
division, turned to outside suppliers
key hardware and software and
ed up computer stores to sell the
machines.

the process, IBM inadvertently
ed kingmaker. Intel Corp. got the
ochip order. Tiny Microsoft, then a
year-old startup run by a 25-year-old
s, was selected to provide the ma-
e's programming language and oper-
g system. Sears, Roebuck & Co. and
puterLand Corp. were chosen to sell
PC. By the mid-1980s, the new kings
e taking control of the personal-com-
r castle. Intel and Microsoft—more
IBM or any of its clones—began to
rmine how PC technology progressed
to a large degree, how much PCs
ld cost.

lost control. Instead of taking their
ng cues from Big Blue, as minicom-
r and mainframe makers had al-
s done, the unruly mob of PC clone-
ers slashed prices to as much as 30%
w IBM's. To try to shore up sales,
computer giant in 1987 went after
copycats with the PS/2, a more
e-proof design that uses the propri-
y Micro Channel Architecture.

ie new IBM machines made a big
sh. But by then the original PC stan-
—in the slightly updated PC AT for-
—had become a force that even IBM
dn't stop. The clonemakers contin-
to build sales and market share by

Apple is feeling the pinch, too. It has
successfully repulsed all efforts to clone
the proprietary Macintosh design. That
helped the company pile up earnings but
left it isolated in a market that preferred
a standard such as the IBM design—and
limited its share of that market to about
12% in 1990. Late last year, Apple shift-
ed gears. To build market share, it came
up with a cheap computer, the \$999 Mac-
intosh Classic. "If we were going to be a
strong player at the end of the decade,
we had to have more than a 12% share,"
says Bob Puette, president of Apple USA.

The strategy worked—in a way.
Puette thinks Apple will finish 1991 with
a 19% share of PC shipments. But profits
have nosedived: Not only are the Clas-
sics themselves less profitable, but they
also have stolen sales from Apple's high-
er-margin computers. So Apple recently
announced its biggest layoff ever—
about 1,500 employees—and in the June
quarter posted a \$53.1 million loss.

'THIS IS GEOPOLITICS.' These develop-
ments are what pushed IBM and Apple to
hammer out their startling alliance. If
they can lay out a new standard—on
their own terms—they hope to regain
industry leadership and restore the type
of profit margins that go to the players
that control the standards. Their vision
for PCs? Computers based on IBM's own
RISC microprocessor, and on Apple's
ground-breaking work in software. The
result: desktop computers that are
speedier, more colorful, more reliable,
and that come with far better software
than the PCs of the 1980s.

But influential as they are—between
them, Apple and IBM control more than
30% of the market—the new teammates
are by no means guaranteed the leader-
ship slot in the coming PC era. Because
the desktop computer market has be-
come so vast, all sorts of computer mak-
ers are fighting for the role. Worksta-
tion makers such as Sun Microsystems
and Hewlett-Packard Co. already sell
high-powered machines much like the

improving on the older
standard. As IBM's
share dropped, from
27% in 1985 to 16.5%
last year, according to
International Data
Corp., the company
began to compete on
price. In the first half
of 1991, IBM lopped as
much as 25% off its
PS/2s in three rounds
of price cuts. "IBM has
billions of dollars in
profits missing" be-
cause its PC design is
so easily cloned, says
Gates.



JIM MANZI

CEO, LOTUS DEVELOPMENT

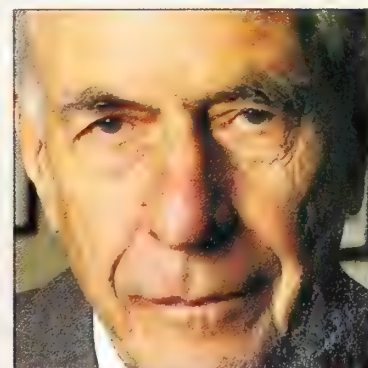
"The PC is the single biggest way I
communicate. But I'm not one of
those manic people who think if you
haven't sent 700 messages that day
you're not a he-man."



LESTER THUROW

DEAN, MIT'S SLOAN SCHOOL
OF MANAGEMENT

"I would no sooner go back to a
typewriter than I would to pencil
and paper. I think there's a mystery
here. Why do we have all these
wondrous things and productivity
gains aren't showing up?"



JOHN KENNETH GALBRAITH

ECONOMIST, HARVARD UNIVERSITY

"I write longhand partly out of habit,
partly because I imagine I get a
smoother, more liquid flow of words.
And there is compelling evidence
on my side. Did Shakespeare,
Dante, or Mark Twain have a PC?"

PCs that IBM and Apple envision. Suppliers such as Digital Equipment Corp., which blew it in the first PC era, are looking for a second chance. And companies such as Compaq Computer Corp., which blossomed by cloning the PC, are determined to stay on top by helping to forge the next industry standard. "We're entering a period of more change than ever before," says Rod Canion, Compaq's chief executive.

And it won't be a smooth transition. "There is a new battle royal forming," says Robert Metcalfe, who developed Ethernet, the industry's networking standard. Computer and software makers began choosing sides for the battle well before the IBM-Apple linkup was announced. IBM itself has teamed up with a host of software makers, including PC networking leader Novell Inc. Compaq has allied with DEC and some 60 other companies to support a proposed RISC-based PC standard.

What's more, nearly every U.S. PC maker has lined up a Japanese ally to

supply critical technologies for making laptop and notebook computers. "Everyone has so much trepidation about their place in the future that they're trying to lower their risks by lining up support," says Peter J. Rogers, an analyst at San Francisco investment bank Robertson Stephens & Co. Echoes Jim P. Manzi, Lotus Development Corp.'s CEO: "This is not just technology. This is geopolitics."

BUILDING BLOCKS. Much of the battle is being fought over software. Future operating systems—which provide PCs with their basic instructions—must be able to manage handwriting, video, graphics, voice, and text, all of which will be flowing over computer networks. What's not clear is which company will provide that operating system (table, page 64). Microsoft is trying to engineer those capabilities into its existing Windows graphics program. Windows now is sold as an add-on to give PCs and clones running Microsoft's 10-year-old MS-DOS operating system a look and feel

similar to Apple's Macintosh. In 1992, Microsoft says it will supplant MS-DOS with NT, for New Technology, a new operating system that will let PC owners do many things at once, and make use of RISC microprocessors.

The Microsoft approach is evolutionary—Windows and the application programs written for it will remain the same, but the underlying operating system will be upgraded. IBM and Apple are taking a far bolder tack. Instead of upgrading old operating system technology, as Microsoft is doing with Windows, they're betting on a whole new approach. Known as object-oriented programming, this method involves building programs from interchangeable blocks of prefabricated computer code called objects. Object programming will help computers accommodate new multimedia technology and could allow ordinary office workers to create custom programs.

Such advances can't come soon enough. Lately, the PC business has been

MULTIMEDIA COMPUTING: PCs THAT DO EVERYTHING BUT WALK THE DOG

If there's one thing just about every pundit agrees on concerning the future of the personal computer, it's that it will have a "multimedia" personality. That is, it's going to deal with humans by using more than just green or amber text and simplistic bar graphs. Tomorrow's multimedia computer will add color video images and hi-fi stereo sound. It will synthesize human speech, turn the results of scientific experiments into animated pictures, and even improvise jazz. With everything from *Citizen Kane* and *Mood Indigo* to simulated car crashes and DNA chains available in digital form, the multimedia computer is going to open windows into a vast new world of information and entertainment.

Which is just what the stagnating PC industry is looking for right now—a big dose of show biz, to make computers easier to use and alluring to a mass-consumer market. Perhaps 25% of the U.S. population regularly uses computers now, because the machines are either too difficult to run or too limited in reach. Multimedia technology, though, promises to help even the illiterate participate in the Information Age. In Tulare County, Calif., farm workers are signing up for social services on touch-screen PCs that show digitized video clips in English, Spanish, and four Southeast Asian languages.

The PC business today is "like the motion picture industry before sound," says Peter Black, president of Xiphias, a Los Angeles developer of compact multimedia disks. The trouble is that no one's quite sure what type of multimedia machine will unleash the new market by setting a software standard that will encourage production of pre-recorded program material. Will it be a souped-up version of today's IBM PC or Apple Macintosh? Or an entirely new kind of computer, designed just for multimedia use? Or, perhaps, some home-TV add-on for affluent couch potatoes? Should this new machine be sold in computer stores, electronics shops, or mass merchandisers? Where will you shop for multimedia disks?

Indeed, nobody can say for sure what the term multimedia really means—except for some vague commingling of television and computing. "It's like pornography," says Nick Arnett, president and chief analyst of Multimedia Computing Corp., a market researcher in Santa Clara, Calif. "You know it when you see it." Or hear it. But that's not preventing

anyone from projecting a market of cinematic proportions: Inteco Corp., a research house in Norwalk, Conn., estimates that from a \$4.68 billion market in the U.S. in 1991, multimedia PC sales will balloon to \$22 billion by 1995.

For now, the most intriguing multimedia systems are being customized for industrial training, education, and public information kiosks. Cornell University medical students learn pathology on Macs connected to optical disks full of text, detailed drawings, and animated sequences. High school students now study Tennessee's poem *Ulysses* on a desktop computer. Or, to a videodisk player, you can browse through a library of readings and analyses, including a segment on Shakespeare's relationship with his songs.

BONANZA. For "power users"—scientists, intelligence analysts, and engineers—the technology will be indispensable to interpreting floods of information. Teams of researchers

A laser-disk encyclopedia might have voices, video, and sound to accompany the usual text and drawings

across the globe will one day be able to talk with and see each other, share electronic-blackboard scribbles, and watch films generated from experiments all via a network of desktop computers.

The elusive bonanza, though, is the mass market. Virtually every source of information into the home—cassette videotapes, floppy disks, books, and

DIAL-A-VIDEO DATA SERVICES

NEW
PC
UPDATES

In the 1990s, PCs that can display television-quality pictures will dial into on-line services to call up digitized clips from audio-video libraries. After searching an index and paying a fee, school kids studying space could download, say,



footage of a space shuttle launch. All this will be possible with ultra-high-capacity phone lines and audio-video compression technology

wing its age. Just a few years ago, the industry's annual growth rate was tear-ahead at a 37% annual clip, according to IDC Corp. Now, the market researcher figures, worldwide sales grow just 15% in 1991. In the U.S., growth will be more modest—8%. Other analysts aren't predicting growth at all.

The recession gets the blame for the slowdown. But after summing 75 million IBM-compatible PCs, the U.S. market is approaching saturation. Big businesses gorged on PCs in the mid-1980s, and by the end of the decade most small businesses were using PCs, too. Without new customers—or compelling new uses that require updated hardware—the PC industry risks be-

enhancing older models, says market researcher Inteco Corp.

One obvious solution is to drum up new buyers. And one great undercultivated market remains: ordinary consumers. The goal, says Intel Senior Vice-President David L. House, is to turn PCs into "the calculator of the '90s." Some of

coming largely a low-margin replacement business. "We just do not see the requirement to go out and spend a lot more money," says Dennis Kavanaugh, a technical director for Pacific Bell, which already has about 40,000 PCs installed for its 60,000 employees. Indeed, of the \$55 billion in new machines that will be purchased in the U.S. this year, about 62% will be replacing or

the products to do that are already appearing. Last April, Hewlett-Packard introduced a \$699 pocket-size PC clone that comes with Lotus 1-2-3 built in and that, with a \$400 option, will be able to relay data by cellular phone. And although the first pentop PCs are geared to blue-collar workers and other business uses, they may also expand the consumer market.

PIZZAZZ. Perhaps the most promising possibility is the combination of computers and home-entertainment technology in multimedia systems. Already, suppliers such as Commodore, Philips, and Tandy are marketing systems combining personal computers with compact-disk players that can fetch digitized snippets of sound and video.

These are the kinds of products that could finally give humble PCs the pizzazz they need to conquer the home front. However, they are also the machines that could open up a new contest between PC makers and consumer-electronics companies—in a battle that could make the bruising clone wars of



ENTERTAINMENT: THE PC, CD, AND TV MERGE INTO ONE IN COMMODORE'S HOME CENTER

lio, CDs, or even the telephone—for the multimedia mill. As a result, here's a momentous battle shaping up between U.S. and Japanese manufacturers over the digitized future. The top leads in computers and software put the Japanese electronics giant Sony better positioned for the future of computing, consumer electronics, and entertainment. Matsushita Electric Industrial Co. and Sony, for instance, are leaders in home electronics, and they now also own U.S. entertainment companies

to pump out film and audio material.

The Japanese threat, say many industry watchers, is part of what prompted IBM to team up with Apple. By making Apple its multimedia partner, IBM is keeping Apple from forging stronger ties with Sony.

As in VCRs, the progress of the home multimedia business will be contingent on well-established standards. In addition to the IBM-Apple team, Microsoft Corp. and Tandy Corp. are forging a standard for PC-based multimedia systems. Microsoft is giving its Windows

program the ability to record sound and play audio CDs, for instance. Dutch giant Philips Consumer Electronics, with help from Sony and Matsushita, is pushing CDI, its own format for multimedia disks.

This fall will see the first attempts to create a mass market. Tandy has introduced a multimedia PC, and Philips plans to start selling a CDI computer. Its laser disks include video segments, sound, text, and images, and software to coordinate them. A typical use: multimedia encyclopedias. Commodore International Ltd. is already selling CDTV. The \$1,000 player incorporates a computer but plugs into any TV and resembles a VCR. It's controlled by a remote keypad. One early disk: "Scary Poems for Rotten Kids," which, with pictures, English and Spanish text, and audio, teaches language skills and explores childhood fears. David Rosen, Commodore's director of international marketing, calls CDTV the "Trojan horse" that will get computers into the home.

Watching closely will be Microsoft, IBM, Sony, and Apple, among others, which are expected to flesh out their own multimedia strategies and product lines next year. These companies will be looking to see if Philips' and Commodore's multimedia formats sell. With the market potential for multimedia seemingly so vast, no one wants to get stuck on the losing side of the next Betamax-vs.-VHS format battle.

By John W. Verity, with Sunita Wadekar-Bhargava, in New York, and bureau reports

the 1980s look like a minor skirmish.

By pushing into consumer electronics, computer makers will be taking on Japanese giants such as Toshiba, Sony, Matsushita, and Hitachi. Many of these companies have already made inroads in the computer market with laptops, which favor their skills in building miniature machines and flat-panel screens. Multimedia could give them another leg up. If multimedia turns PCs into consumer electronics, says analyst Rogers of Robertson Stephens, the Japanese could edge out traditional PC leaders. "With consumers, Sony is the preferred brand name. IBM isn't," he says.

Even in well-established markets, PC makers will have far more difficult marketing problems to contend with in the coming decade. The most formidable is finding a way to move beyond the old IBM standard. As the continuing strength of IBM's 30-year-old mainframe design proves, old standards don't die easily.

The problem is inertia. Intel estimates that customers have sunk \$340 billion into Intel-based computers—mostly PCs and clones—and related software. While the workstation market has switched over to lightning-fast RISC microprocessors, PCs remain stubbornly rooted in the original Intel design. By cramming more and more circuits onto new versions of its 8086-family chips, Intel has constantly improved PC performance. Now a \$3.9 billion company, it has the money to keep pushing the limits of the older chip technology. That will make it tough—even for the IBM-Apple team—to displace Intel with RISC technology.

But IBM and Apple—and any other would-be standards-setters—face an even bigger barrier: Microsoft's MS-DOS. After 10 years, Microsoft has sold 70 million copies of the basic PC software—and countless others have been pirated. Tiny Microsoft has grown into the world's largest software company, and its founder, Bill Gates, has become a billionaire—more than four times over. By now, according to some estimates, PC owners have bought nearly 200 million applications programs to run on the MS-DOS operating system. That may put Microsoft in the catbird seat of all time.

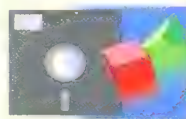
Microsoft's clout—

and the in-your-face way with which Gates wields it—has already created a tremendous rift in the industry. For nearly a year, IBM and Microsoft have been fighting over what technology should succeed MS-DOS. The two companies jointly developed the OS/2 operating system, which they announced in 1987 and said would replace MS-DOS. After three years of massively disappointing OS/2 sales—only 600,000 copies have been sold—Microsoft began pushing its Windows graphics program instead of OS/2. Since then, more than 4 million copies of Windows have been purchased.

PAINLESS PROGRESS. The OS/2 debacle did drive home an important lesson for the PC industry. It showed IBM and the rest that customers won't switch if it's too costly. They balked at OS/2 because it would not easily run the programs that they were using on their MS-DOS computers. That meant for big customers to upgrade their PCs with OS/2, they would have had to buy millions of dollars worth of new applications programs such as spreadsheets and word processing programs, transfer old data into new forms, and then retrain their employees to use the stuff. Few were willing to do so.

This time around, IBM, Apple, and the

If you don't like the way your word processing program integrates graphics, you'll soon be able to fix the problem. In the 1990s, advances in programming languages will make it possible for folks who can't program their VCRs to customize software. The breakthrough, object-oriented technology, reduces programs to discrete building blocks of preprogrammed



code that PC owners can string together

will become less and less visible to user."

That will surely help. Right now, however, PC buyers aren't rushing to any of the vaunted new technologies. Until they see that they aren't giving up more than they get, the majority are likely to stick with what they've got. Indeed, say some influential buyers, what they want is more bells and whistles. They want a plain old PC made more usable. John Loewenberg, chief information officer at Aetna Life & Casualty Co., where 80% of the 50,000 workers have a PC on their desk, says today's typical PC "is a study in user hostility." He wants suppliers to make PCs easier to use, software simpler to learn. Lawrence Bacon, chief information officer at Travelers Corp., says his personal computer won't be truly useful until they're simple enough for impatient top executives to master. As things stand now, "if executives can only get 20% of what they need from the PC, the rest has to come from other sources they're not going to master," Bacon says.

That's the ultimate challenge. No new technology—not even if dreamed up by the industry's top two suppliers—will make a difference in the new era if it doesn't make personal computers easier to use with. The IBM PC and the ornery software that made it so difficult to master became commodities long ago. Ten years later, the thrill is gone.

By Deidre A. Depken
New York and Richard
Brandt in San Francisco
with bureau reports

SOFTWARE WARS: THE BATTLE FOR THE NEXT GENERATION

The current generation of operating systems, or basic control programs, is still in its infancy. But computer and software makers are already promising the next great leap forward.

MICROSOFT

Now Its popular Windows 3.0 graphics program has given new life to the venerable MS-DOS. But MS-DOS now works only on Intel chips and does one task at a time.

Mid-1990s NT, for New Technology, will incorporate Windows, work on RISC computers, and do many jobs at once. It is also expected to have multimedia capabilities

IBM

Now A multitasking system called OS/2 2.0 is due out this year. It will run MS-DOS and Windows programs as well as new OS/2 software.

Mid-1990s Starting last year, when it formed a joint venture with Metaphor Computer Systems, IBM has been working on object-oriented programming to smooth over differences among operating systems

DATA. BW

APPLE

Now Recently released System 7, an important update of the Macintosh operating system that allows applications to share data easily.

Mid-1990s The Pink project promises to be Apple's first operating system to work on non-Macintosh computers. It should run Mac, OS/2, and certain Unix programs. The work will likely be combined with IBM's

AN ALAN LADD JR. WAKE LEO THE LION ROAR?

is a hitmaker—but MGM's legal and financial woes are legion

After 5 p.m. on Friday, but executives still cluster outside the office of Alan Ladd Jr., chairman of MGM-United Artists Corp. Emerging between meetings, Ladd is dressed casually in blue jeans and a pink sports shirt. But his expression is somber. He is back from New York, monitoring sneak previews of the upcoming release, *Harley Davidson and the Marlboro Man*, with Mickey Rourke and Don Johnson. Asked how the film will do, he crinkles his nose. The

future ahead holds little prospect for betheer: Ladd has days of deposits scheduled in connection with law-suits sparked by the merger of MGM's ex-chairman, flamboyant Italian financier Carlo Parretti. Ladd has a bad cold, and normally serene takes on a haggard look.

For Laddie. He's Hercules clean-up the stables," says David Gerber, time friend and of MGM's television unit. "Everywhere he looks, he's more manly." Ladd, the 53-

old son of the movie star, is being asked to resurrect the fortunes of the great MGM studio at a time when its future seems as murky as the Los Angeles skies. MGM was nearly pushed into bankruptcy in April before its chief creditor, Crédit Lyonnais Bank Nederland, sold out Parretti and installed Ladd. Since, Crédit Lyonnais has doled out only the barest amounts of money needed to make films. Yet Ladd remains under pressure to come up with hits, and to brace up the studio for resale.

Ladd, famous as the studio executive who helped George Lucas make Luke Skywalker a household name, has hit high spots before. Tussles with Twentieth-Century-Fox Film Corp. Chairman

Dennis C. Stanfill and later with Kirk Kerkorian when the financier owned MGM drove him to leave both studios. But his current challenge includes a legal fight: Parretti's suit against Crédit Lyonnais names Ladd as a defendant and alleges a backroom plot to drive the dealmaker from the company, which Parretti bought from Kerkorian for \$1.3 billion last November.

Parretti's aides say it's not really Ladd they blame. But Ladd allows that

Driving Miss Daisy producer Richard D. Zanuck, Mel Brooks, and Lucas have followed him from studio to studio. The *Star Wars* trilogy Ladd brought to Fox funneled more than \$500 million into a nearly moribund studio. He also won Academy Award nominations for *Julia*, *The Turning Point*, and *Norma Rae*. At MGM from 1986 to 1988, he brought the studio two of its few recent hits, *Moonstruck* and *A Fish Called Wanda*.

RETIRING SORT. If Hollywood complains at all about Ladd, it's that he's too soft-spoken. Some joke that he whispers to make people lean forward. Friends say he's just a retiring sort. He prefers quiet dinners at his Beverly Hills home to the Hollywood party circuit. For vacation, he generally escapes with his second wife and daughter to the Kahala Hilton in Hawaii. He's also a big sports fan who not infrequently watches three sports programs at once on television.

Ladd's reputation for giving produc-

ALAN LADD JR.'S TRACK RECORD

BOX-OFFICE HITS...

Gross receipts (millions)

THELMA & LOUISE 1991	\$38.2*
MOONSTRUCK 1987	80.6
NINE TO FIVE 1980	103.0
STAR WARS 1977	322.0
YOUNG FRANKENSTEIN 1974	76.0

...AND MISSES

NOT WITHOUT MY DAUGHTER 1991	\$14.8
QUIGLEY DOWN UNDER 1990	21.4
THE RIGHT STUFF 1983	21.2
BLADE RUNNER 1982	27.4

*Still in theaters

DATA: BW, ENTERTAINMENT DATA INC.



the legal battle, combined with MGM's money woes, has had repercussions. Parretti is seeking to be reinstated as chairman, and producers are wary of a company whose future is uncertain. A spate of unpaid bills earlier also drove away some producers, who worried that MGM wouldn't have the cash to pay them or to release their films. And a shortage of advertising funds forced MGM to delay release of a dozen films, including *Thelma & Louise*, which Ladd says would have grossed \$20 million more if released earlier. So far, Ladd has been able to line up only three films for 1992, far short of his goal of 8 to 12.

The best thing Ladd has going for him is his own record. Big names such as

others great freedom attracts them even in the face of adversity. Lucas says he brought his 1988 film *Willow* to MGM solely because of Ladd. When Paramount Pictures wouldn't pay the nearly \$17 million Zanuck needed to make his newest film, *Rush*, the producer took it to Ladd, despite MGM's troubles. "Laddie's word is his bond," says Zanuck, who double-dated with Ladd in college.

Ladd is one of Hollywood's few native sons. His father appeared in 47 films, including the 1953 classic *Shane*. But Laddie's boyhood was uncommonly rough. He lived with his mother after his parents divorced, but her frail health later forced him back to his heavy-drinking father. The father died from an over-

dose of sedatives and alcohol when his son was 26. Ladd calls their relationship "basically nonexistent"—but all along, he was drawn to films, seeing as many as 18 in a week. "I should probably see a shrink, although I know it was probably to win my father's approval," he says of the obsession.

Even so, Ladd initially avoided show biz, trying his hand at real estate management. But he gravitated toward film, first as an agent, with such clients as the young Robert Redford. After four years in London as a producer, he joined Fox, and by 1977 was studio president. He left in a huff in 1979, when then-Chairman Stanfill refused to pay Fox executives bonuses.

MGM is a homecoming of sorts for Ladd. While running the studio in the mid-1980s, he tried to buy it, but he couldn't get the financing. He later became furious when Kerkorian tried to sell MGM to producers Peter Guber and Jon Peters without informing Ladd. His anger led to a confrontation in an MGM elevator, in which he uncharacteristically hollered at Kerkorian. Ladd quit the following year, 1988, when Kerkorian tried to pare expenses by firing all the producers Ladd had brought to the studio.

ROLLER COASTER. Within six months, Ladd had traded one difficult financier for another: He wound up at Parretti's Pathe, which was soon to buy MGM. Granted freedom to make whatever films he wanted, Ladd signed a four-year contract as producer that promised him at least \$2.5 million a year in salary and \$125 million a year for production. Friends were skeptical about Parretti, but Ladd wanted a change: "I had played it conservatively for most of my life. I thought it was time to try the roller coaster."

That coaster crashed early this year, three months after Parretti bought MGM. Ladd considered quitting because of unpaid bills, but opted to stay after Crédit Lyonnais provided a cash infusion—and gave him a new four-year, \$3.2 million-a-year contract. Now, he's negotiating to increase funds for production. So far he has lined up Zanuck to do another film, *Rich in Love*. And producer Albert "Cubbie" Broccoli may do a James Bond movie for the studio. Ten other films, in the can but sitting on the shelf because of financial problems, are scheduled for release in the next few months.

Ladd concedes it's tough, emotionally, to groom the old MGM lion just to sell it off. But he has no choice. Already, he says, he has talked with two potential Japanese buyers and knows of other interested parties. Ladd no longer harbors ambitions to buy MGM himself, though. After the rough couple of months he's been through, no one can blame him.

By Ronald Grover in Los Angeles

Media



CABLE TV

WHY CABLE COMPANIES ARE PLAYING SO ROUGH

They're terrified of the Baby Bells and other high-tech rivals

For years, the cable-television establishment seemed to have everything wired. It persuaded state and local lawmakers to write stiff rules for upstart cable companies trying to break into their monopoly franchises. And it thwarted a congressional drive last year to place new curbs on established cable operators, even though consumers were raising hell about skyrocketing rates and poor service.

But on July 25, the future of the \$18 billion cable business began to slip out of the industry's hands. U.S. District Judge Harold H. Greene lifted regulations that barred the seven regional Bell telephone companies from entering the information-services business. Greene's ruling means the Baby Bells can use their phone lines to offer services such as home shopping and banking. Now, lobbyists say it's only a matter of time before Congress allows phone companies to compete directly with cable by offering television programs.

That's a scary prospect for the industry, which is already under attack from new technology such as direct-broadcast

satellites and wireless cable, and from upstart rivals within the business (table). Worse, all these threats are coming. Cable's days of torrid growth are ending. While 90% of U.S. homes can receive cable, only 60% subscribe. That means just about everybody who wants cable already gets it. The slackening appeal has slowed cable's annual revenue growth from 38% in 1980 to 13% in 1990.

TOUGH GUYS. To stem the tide, the industry is resorting to some rough tactics. Besides heavy-duty lobbying, cable operators are using hardball marketing campaigns to quell competition. To snuff out the new technology, they're denying rivals access to programming. "The guys are the NRA of the video age," says Harry P. Cushing, president of TeleCablevision Inc., which has been taking over established cable services in Florida.

Like the National Rifle Assn., the cable industry is a powerful Washington player. Last year, its trade group, the National Cable Television Assn., sponsored a popular measure that would have allowed cities to impose tough regulations on cable franchises. The NA

ed Senator Timothy E. Wirth (D-), whose state is home to several cable companies, to bury the meat at least for now.

ch past legislative victories may something to the \$565,000 that the lavished on congressional campaigns in the last election. But stopping Baby Bells is another matter. For thing, the Bush Administration, opposed tougher cable regulation, letting phone companies into the mess. It didn't help when the General Accounting Office reported on July 18 rates have ballooned 61% since deregulation in 1986.

ole operators are terrified of the Bells because their pervasive network of phone lines gives them access to nearly every household in America. they can use these phone lines to state-of-the-art interactive promoting. That would allow customers select the time and day they want to a specific program simply by ing buttons on a keypad.

TICKS. Such innovations are years. But the cable industry is already ing to offer similar services. Time er Inc., the nation's second-largest supplier, is installing fiber-optic cable in its Queens (N.Y.) system. The technology will allow it to offer in- dvice services, too. Fiber optics also cable to compete with direct- cast technology. DBS, which trans- TV signals via satellite small receiving dishes, offer many more chan- than current cable tech- y. But by using fiber s, Time Warner will be to expand the number annels it can offer in ns from 75 to 150.

er optics may be only ost benign way cable is ng the DBS challenge. s say some cable weights are trying to the technology by og it. Last November, 9 e top 15 cable operators, ing No. 1 Tele-Comm- ons Inc. (TCI), started own DBS service.

e venture, called K e Partners, has several and subscribers in 40 arkets. But critics say by pooling so many big rs, K Prime could even r swamp any competing ms. Moreover, they say partners are eting K Prime as a supplement

to their basic cable service rather than as a rival technology. Nine states and the U.S. Justice Dept. are scrutinizing the venture to determine if it violates antitrust law. K Prime's executive vice-president, David P. Beddow, insists it isn't anticompetitive.

Perhaps the most powerful weapon the industry has to thwart competition is

The cable operators' strongest weapon: A virtual lock on programming

its virtual lock on programming. Several big cable-franchise holders also own programming companies. Time Warner, for example, is one of Hollywood's largest TV programmers through its HBO, Warner Bros., and Lorimar Television divisions. By limiting access to shows, cable operators can leave rivals with little desirable programming to bounce off their satellites or to send over their phone lines.

Take Sky Cable, a DBS venture backed by Rupert Murdoch's News Corp., General Motors' Hughes Communications, NBC, and Cablevision Systems. The project ground to a virtual halt in June, largely because the partners feared they wouldn't have access to programs. The

cable industry says it should be able to sell shows to whomever it pleases.

If competition from outsiders isn't enough, established cable franchises face a growing threat from new cable operators. Since 1989, the number of cities with competing cable companies has doubled, to about 50. But that growth hasn't come without a fight. When Telesat applied for a cable-TV license for Cape Coral, Fla., in 1988, incumbent franchisee Cablevision Industries counterattacked with a blistering ad and letter campaign. It claimed that Telesat would damage or destroy hundreds of trees by erecting poles to string its cable. Telesat finally prevailed after a heated six-hour city council meeting that lasted until 1 a.m.

When efforts to block rivals fail, some cable companies resort to bare-knuckles marketing tactics. Pacific West Cable Co. sued Scripps Howard Co.'s Sacramento Cable in 1989—charging that after Pacific West received a franchise in Sacramento in 1989, Sacramento Cable slashed rates, offered free service, and gave away TVs in areas where Pacific West had laid cable. Pacific West claims Sacramento Cable employees followed its salespeople door-to-door and disrupted their efforts to sign up customers. Scripps settled the suit on Apr. 8 by agreeing to pay Pacific West \$12 million.

Cable operators are using more subtle public relations techniques as the industry redoubles its campaign against new regulations. In June, 1990, Cleveland's *The Plain Dealer* published an article by an apparently independent expert blasting the legislation. But Ohio University economics Professor Richard K. Vedder was paid \$1,000 to write the piece by public-relations man James M. Savarese. Savarese, who works for the cable industry, even vetted the article so that it hewed to the party line. Vedder says he should have disclosed the link: "Maybe I was a little naive." Savarese couldn't be reached for comment.

Such tactics won't burnish cable's reputation. That could prove costly when measures to free the phone companies are tossed into the legislative hopper. With the Baby Bells poised to enter the fray, cable will need all the allies it can get.

By Mark Lewyn in Washington

MORE STATIC

Cable franchises are lucrative—and under attack:

THE THREAT

Phone companies that want laws letting them deliver TV programming via phone lines. On July 25, a federal judge allowed them to start offering home shopping and banking

Direct-broadcast satellites and microwave cable that deliver hundreds of channels

Rival cable operators that want to horn in on existing local monopolies. The number of cities with competing cable systems has doubled since 1989

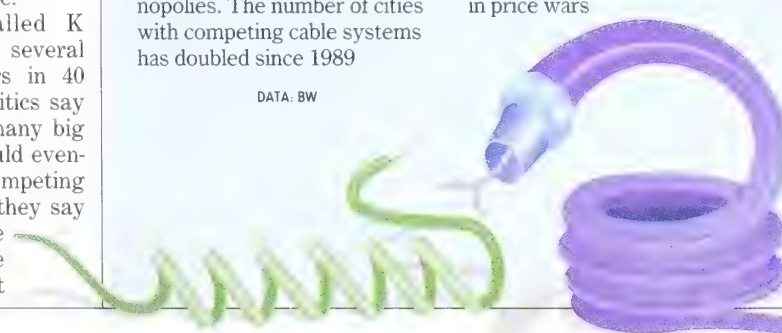
THE RESPONSE

Make campaign contributions to key members of Congress hoping to influence legislation. Install fiber-optic wire, wire that also delivers interactive service

Keep a tight rein on programming and start rival joint ventures in direct broadcast

Lobby for stiff restrictions on newcomers and drive them out in price wars

DATA: BW



DID WESTINGHOUSE KEEP MUM ON PCBs?

A new lawsuit charges that it knew of health risks it didn't disclose

When the Environmental Protection Agency banned polychlorinated biphenyls (PCBs) in 1979, it probably came too late for Richard K. Sluder of Bloomington, Ind. The former Westinghouse Electric Corp. worker blames his debilitating arthritis and memory loss on PCBs, which he says drenched him daily on the job for years. Sluder, 39, is a likely candidate to suffer some ill effects: At one point, his blood had the highest PCB concentration ever recorded in a human—3,450 parts per billion.

In a suit filed last March, Sluder and eight other Bloomington workers charge Monsanto Chemical Co., the sole U.S. producer of PCBs, and Westinghouse with fraud and battery. Sluder is one of roughly 1,000 claimants to file PCB-related personal-injury suits pending against Westinghouse. In many of those cases, Westinghouse has had the upper hand, since the scientific link between PCBs and human illness is unproven. But Sluder's suit comes at a time of mounting scientific evidence linking PCBs to cancer and other ailments. And the case is the first to charge that Westinghouse exposed its workers to chemicals it knew were unsafe. "We have documented evidence of exposure levels, which is unprecedented," says Sluder's lawyer, David S. McCrae. "Westinghouse knew these chemicals would poison the workers and cause death. But Westinghouse said nothing."

Westinghouse spokesperson Christopher C. Newton says the company gave workers protective clothing and took other safety steps. Newton won't say whether Westinghouse told the workers

directly about the risks of PCBs, but he adds that they were free to raise health concerns during monthly safety meetings. Westinghouse and Monsanto say studies have never conclusively linked PCBs to health problems other than skin rashes. Thomas M. Bistline, Monsanto's assistant general counsel, labels the Sluder suit "a scurrilous fabrication."

Unlike other suits, Sluder's case relies on new medical tests and internal Westinghouse memoranda addressing corporate concern over the safety of PCBs. If Sluder can prove that the company believed PCBs were potentially harmful yet failed to take adequate safety precautions for its workers, he could establish a legal precedent for pending litigation against Westinghouse and other companies that used PCBs.

From the 1930s to 1979, Westinghouse and General Electric Co. were the biggest purchasers of PCBs as fire retardants and coolants in capacitors and transformers. Other big users have included electrical-equipment companies such as McGraw Edison, ITE Imperial, and Sprague Electric. NCR used PCBs to make carbonless copy paper. Though no firm number is available, plaintiffs' attorneys estimate that tens of thousands of workers have handled PCBs.

The health studies are anything but conclusive. In 1977 and 1985, the National Institute for Occupational Safety & Health conducted two Bloomington worker studies that found no direct link between PCBs and current medical ailments—a finding that NIOSH admits may be flawed. And a 1988 review of scientific literature by Renate D. Kimbrough, then director of health



Sluder: At one point, his blood had the most PCBs ever recorded in a human



WESTINGHOUSE CLEANS UP NEAR BLOOM

and risk capabilities at the EPA, concluded that "exposure to PCBs has led to convincing, clinically demonstrated chronic health effects in humans."

But a NIOSH mortality study published in April that reviewed Bloomington workers' causes of death from 1971 to 1977 concluded that plant workers "at excess risk" of dying from skin cancer. It also found that an unusually high number of deaths from brain cancer merits further research.

DILEMMA. While the full extent of human health dangers are still being debated, more and more animal studies link PCBs to numerous illnesses, including cancer, liver damage, and birth defects. The index of suspicion [of health problems in humans] is so high, no one would seriously propose that we not worry about PCBs," says Walter J. Rogan, medical officer at the National Institute of Environmental Health Sciences, a research unit of the National Institutes of Health. And animal studies may now carry more legal weight: In September, 1990, a federal appeals court in Philadelphia ruled that animal studies are admissible as causation evidence in PCB-liability cases.

Beyond the legal issues, the Westinghouse case cuts to the heart of an ethical



THE LONG PCB TRAIL AT WESTINGHOUSE

1947 Westinghouse memo describes severe health hazards of prolonged exposure to polychlorinated biphenyls. Monsanto is the sole producer of PCBs, widely used in industry as insulators, coolants, and lubricants

1957 Westinghouse opens new plant near Bloomington, Ind., to make PCB-containing capacitors

1968 PCBs are investigated worldwide as a likely health hazard and highly toxic pollutant when 1,300 residents of Kyushu, Japan, become ill after eating rice oil with high levels of the chemical

1972 A Westinghouse study finds PCB contamination near its Bloomington plant, but city officials do not learn of the results. Monsanto requires PCB customers such as Westinghouse to sign a waiver relieving it from legal liability for improper uses of the chemical

1973 Bloomington officials learn of PCB dangers at an EPA conference in Chicago, and a city chemist requests a government survey. Testing reveals PCBs in city sewer system. Environmental Protection Agency identifies Westinghouse as one of 37 major sources of PCBs in the U.S.

1981 Bloomington finds PCBs in new landfills. Local salvager becomes one of the first of some 1,000 claimants to sue Westinghouse over health problems from PCBs. Monsanto also gets sued

1980 A draft federal study shows that Westinghouse workers exposed to PCBs are at higher risk of dying from skin cancer and notes unusually high number of deaths from brain cancer

1991 In a suit, nine workers allege that Westinghouse and Monsanto exposed them to PCBs but didn't disclose the health risks. The companies dispute the charges. The federal study is published. Westinghouse and city still fighting over cleanup

DATA: BW

ULD BE MORE THAN \$1 BILLION

ma that corporate decision-makers face: Do they openly discuss the health hazards of chemicals or ologies and risk exposing their anies to financially crippling liabilities? Or do they keep mum until all evidence is in? Westinghouse's New-epies: "In our view, corporations d provide employees information rning the safe use of all industrial rials and chemicals. PCBs are and no exception." Says Monsanto at-y Bistline: "We have disclosed what new when we knew it."

cern about workers' health after ure to PCBs and other chemicals o the 1985 Occupational Safety & th Administration right-to-know which requires employers to tell ers in advance of potential health of industrial chemicals. But even companies comply, OSHA admits workers have trouble understand- e complex scientific disclosures.

estinghouse has been grappling uncertainty over PCBs for two de- in Bloomington, a bucolic college 50 miles south of Indianapolis and ome of Westinghouse's capacitor since 1957. PCBs had been widely in industry since the 1930s as insu-

lators, coolants, and lubricants. But it wasn't until 1966 that Swedish scientists identified PCBs as likely toxic pollutants because they degrade slowly and build up in animal tissue and blood. Sentiment dramatically turned against the chemical in 1968, when 1,300 residents of Kyushu, Japan, became ill after eating PCB-contaminated rice oil. The Japanese suffered skin lesions, eye ailments, nausea, and joint problems. Later, many of the victims' offspring had birth defects.

CLEAN HANDS? In their suit, the workers charge that Westinghouse never told them of potential PCB health hazards. In fact, workers say that when the plant's union local asked the company to discuss PCBs soon after the rice-oil incident, employees were assured that there was no danger. Jason Morrow, a former union local president at the plant, recalls employee meetings in which then-plant-manager Donald M. Sauter "washed his hands and face in what he told workers was liquid PCBs to convince them not to worry." Westinghouse spokesperson Newton confirms that Sauter "dipped his hands" in PCBs at a meeting.

That display of confidence conflicts with several internal Westinghouse memos dating back to 1938 that the

workers rely on in their suit. In a letter dated Sept. 15, 1947, E.C. Barnes of Westinghouse's medical department writes that long-term exposure to PCB fumes "may produce internal bodily injury which may be disabling or could be fatal." Westinghouse will only say that the same description applies to several chemicals used in the plant and that safeguards were adequate.

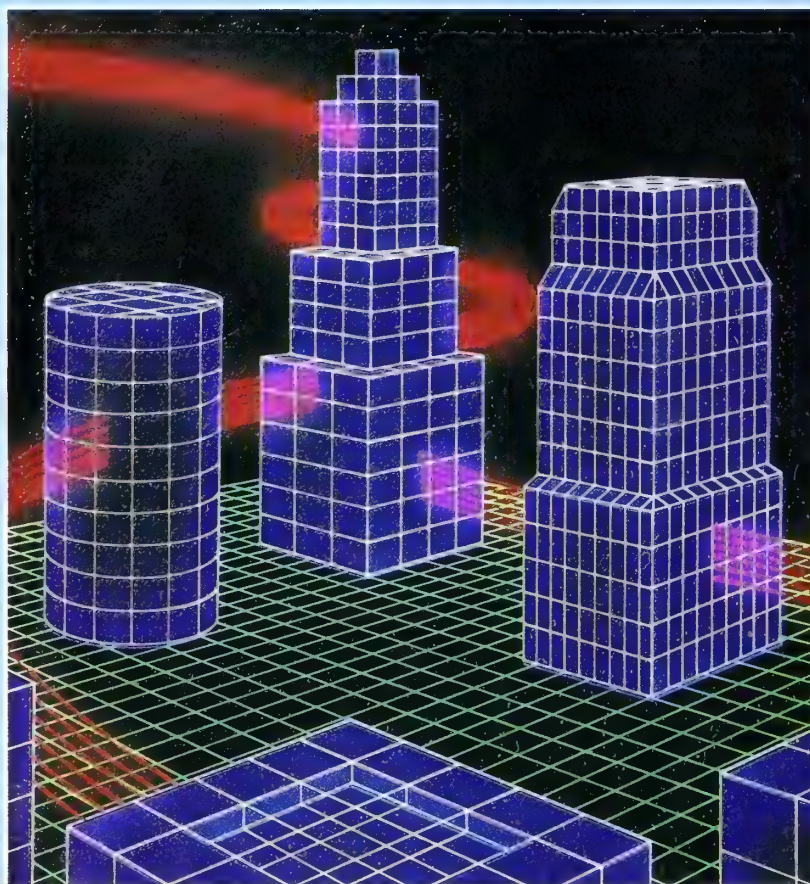
Nevertheless, after the rice-oil incident, some Westinghouse officials, fearing regulatory sanctions and liability suits, ordered an internal study, according to Thomas O. Munson, a former Westinghouse biochemist. Sluder's lawsuit will rely on its findings, in part, to prove concealment. Munson says he performed the confidential study of PCB contamination in 1971-72 near four Westinghouse plants in Indiana, Pennsylvania, and Virginia and then submitted the results to the company. Munson told BUSINESS WEEK he got the go-ahead for the study directly from then-CEO Donald C. Burnham. A Westinghouse spokesperson says the company received only Munson's Bloomington study and that Burnham doesn't recall the conversation.

Of the plants, says Munson, Bloomington had the worst PCB contamination

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including high levels in surrounding areas. He says that in 1972, he urged the manager and his superiors to make the study public and take remedial action. He says Westinghouse ignored his recommendations to remove PCBs from the waste and failed to tell city officials about the contamination. The Westinghouse spokesman says the company did not tell the city because "the findings were not considered disturbing."

Four years later, Bloomington discovered its PCB contamination: After attending an EPA conference on the substance in Chicago, a worried city chemist requested an agency survey. Indiana and other studies since 1976 have shown Bloomington has the nation's largest volume of PCBs—650,000 cubic yards of landfill soil, says John N. Langley, the city's environmental coordinator.

The discovery triggered a flurry of city suits. To settle city, state, and federal actions, Westinghouse agreed to pay for the cleanup—without admitting that it caused the contamination. Bloomington Mayor Tomilea Allison says Westinghouse's cleanup costs in the city could exceed \$1 billion.

Monsanto was worried about suits as early as 1972. The company began

requiring customers, including Westinghouse and GE, to sign agreements relieving it of legal liability in suits arising from improper use of PCBs—putting buyers on notice of possible dangers. In 1977, two years before the federal ban on PCBs went into effect, Monsanto stopped making the chemicals. Westinghouse also quit using PCBs, and in 1989, it sold its capacitor and transformer

Experts say the legal system should be changed so that companies can reveal health risks without facing litigation

plants to Swedish conglomerate Asea Brown Boveri.

Whatever the outcome of the Sluder case, liability experts such as Peter H. Schuck, a Yale law school professor, say the furor over PCBs and other potentially hazardous materials underlines a weakness in the legal system. Other experts argue that companies should be encouraged to reveal possible health risks with-

out facing litigation. That could be tough. "In any kind of reform," says Schuck, "companies are worried about new claims down the road."

Medical monitoring of workers may be an apt remedy for instances where hazards are less certain than those involving such materials as asbestos, say unions and plaintiffs' attorneys. They add that diagnosis and treatment could even trim company liability by cutting medical expenses. But Westinghouse says "there's nothing in the [Sluder] suit that would merit medical monitoring."

Ultimately, Congress may be forced to step in. Unions such as the International Union of Electronic Electrical Salaried Machine & Furniture Workers may soon push for federal legislation mandating medical monitoring. While such programs could stem workers' anxieties about impending sickness or even death, companies say the programs will force them to pay twice—first for the monitoring and then for the personal-injury damages that might accrue. Still, in the absence of any compromise between employees and companies, the tally of worker injuries and liability suits promises to grow.

By Michael Schroeder in Bloomington

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RUGGED REFINEMENT: A 4x4 ROUNDUP

Nowadays, people buy off-road vehicles as much to haul kids and packages through the 'burbs as to ford streams or clamber over boulders. But while they have all the creature comforts of a family sedan, they are definitely not cars.

Off-roaders—also called sport-utility vehicles and 4x4s—have a higher center of gravity and are designed for low-speed maneuvers on varied terrain. So they don't handle like cars, especially in sudden or high-speed turns. Their suspensions are stiff, which can bounce you like a load of bricks over rough pavement at highway speeds. And most don't seat six comfortably.

Still, off-road vehicles are taking over America's roads. They have about twice the cargo space of a Taurus sedan, and the seats are high, for a commanding view of the road. They can tow boats or trailers—or trudge through snow with ease. Their image is rugged—not retro, like the big station wagons they're replacing. The most popular package has four-wheel drive, a six-cylinder engine, automatic transmission, and four doors. Here's a roundup of some leading models.

■ **Jeep Cherokee.** The granddaddy of them all, Jeep is synonymous with off-roading. With its crisp, rugged looks and enormous 4.0-liter in-line six, the Cherokee yearns to career through the wilderness. It comes with a choice of the two dominant four-wheel-drive systems: "shift on the fly," which allows you to switch out of two-wheel drive while you're moving, or a full-time four-wheel-drive system. Among other makes, only the Oldsmobile Bravada and Range Rover also offer a



ISUZU RODEO: THE HANDS-DOWN WINNER ON LOOKS ALONE



JEEP CHEROKEE SPORT: A BARE-BONES VERSION OF THE LIMITED

A COMPARISON OF OFF-ROAD VEHICLES

Model*	Price range**	Horsepower	City/highway mileage
FORD EXPLORER	\$18,224-24,174	155	15/20
ISUZU RODEO	17,759-21,869	120	15/18
JEEP CHEROKEE	16,119-26,725	190	15/20
NISSAN PATHFINDER	19,460-25,140	153	15/18
OLDS BRAVADA	23,795-25,000	160	17/22
RANGE ROVER (V-8)	36,500-47,300	178	13/16
TOYOTA 4RUNNER	18,998-28,822	150	15/18

* 4-door, 4-wheel drive, automatic, six-cylinder

** Excludes taxes, title fees, destination charges

DATA: BW

standard full-time four-wheel drive.

Although the upscale Cherokee Limited edition comes with a full complement of comforts, a bare-bones Sport version is available for those who balk at paying \$20,000 and up. But stripped of such amenities as an outside rear hand mirror and cruise control, the Sport comes across as utilitarian at best.

Next spring, the Jeep Grand Cherokee makes its debut. With about the same dimensions as the current Cherokee, it will be the first updating of the classic since 1984. It also will add a driver's airbag.

■ **Ford Explorer.** Since its launch in early 1990, the Explorer has muscled Cherokee aside for clear supremacy in sport-utility sales. However, its design is imposing. The interior is combined with an exterior offering lots of space for passengers and cargo. It's clean and functional inside, with a panel, and, unlike most off-road vehicles, easy rear seat entry and exit. It also has an array of options, such as a CD player worthy of a luxury sedan. To switch from two-wheel drive to four, you push a button on the dashboard. There are no extra levers to engage and disengage in tandem with the gearshift.

Mazda thinks so highly of the Explorer's quality that it sells a two-door version as the Mazda Navajo.

■ **Oldsmobile Bravada.** General Motors makes three 4x4s from the same basic package. The GMC Jimmy is engineered for the off-road enthusiast, the Chevrolet S10 Blazer appeals to the broad "heart of America," and the Oldsmobile Bravada aims for the upscale buyer. The latter is a direct

The optional leather interior covers even the doors. Backseat is just about the comfortable one around. Important, Olds has give Bravada full-time four-wheel drive. Dropping the wheel-drive option eliminates the confusion some cars have about whether to go into four-wheel drive in rain or only in a heavy storm. It also clears the clutter of a four-wheel-drive low and high levers, making for a cleaner interior design. You'd think that would hurt fuel economy, but Bravada is a standout, along with its GMC and Buick sisters.

Mechanically, what's left is pretty good off-road package. In normal use, the drive sends 65% of the power to rear wheels and 35% to front ones. Lacking any underbody shielding, though, the Bravada isn't a fit for finding a new west Passage.

Oldsmobile Pathfinder. On the road and off, the Pathfinder handles with grace and aplomb. Along the way, offers choices: sport or touring suspension, power or manual gearshifts.

Like the touring setting, tone down the bumps at highway speed, don't assume means a soft ride. Steering feedback and other handling characteristics are as pleasingly car-like. In its quest for a great sound system, though, Nissan has crowded the rear speakers so as to restrict cargo space. And the lock is set on an already-dedicated instrument panel, leaving the front passenger to see it.

Toyota Rodeo. On the exterior alone, the Rodeo is a winner. Front and rear, the factory-built Rodeo adds flair to the usual commanding presence of a 4x4. Unfortunately, the interior designers passed the baton. The instrument panel is boxy enough to give in a mid-'80s Chrysler, the radio is awkwardly placed. There are even '50s-style push-out wing windows in the front, which add to wind



RANGE ROVER HUNTER: COIL SPRINGS FOR MORE BODY ROLL



OLDSMOBILE BRAVADA: THE MOST COMFORTABLE BACKSEAT AROUND



FORD EXPLORER: CLEAR SUPREMACY IN SPORT-UTILITY SALES

Mechanically, too, the Rodeo rounds up Thoroughbreds and mules. The engine delivers the goods, as measured by the speedo and tach, but it complains noisily most of the way, particularly from a cold start. The body is prone to squeaks and rattles, and the rear seats are overly hard.

Toyota 4Runner. The 4Runner's strengths are good mechanicals—particularly the engine and suspension—and a bevy of creature comforts. Its weakness is design. Like the Pathfinder, it uses a narrow metal running board to offset the strenuously high climb from the ground to the vehicle's floor. The board is still too high. Worse, the manual stick shift and four-wheel-drive lever cross like a pair of improperly used chopsticks. It's hard to tell whether you're in high-two, high-four, or low-four drive by feel without checking the dash for the "4WD" light.

Range Rover. This is a distinctive 4x4. Every other maker maintains traction over uneven ground by using a stiff suspension. The Range Rover adds coil springs to every wheel and allows a great deal of body roll. To increase legroom, it makes the rear seat higher instead of moving it back. Instead of linking to the wheels, the hand brake cuts power from the driveline.

Of course, it should be distinctive at these prices. Last year, Range Rover added the \$36,500 Hunter version to its lineup, which otherwise starts at \$43,000. The Hunter, though hardly stripped-down, comes with cloth upholstery and without power seats. The latter is a bother, since the manual seatback adjuster is wedged in too tightly.

The Range Rover is a serious off-roader. Sitting tall, it offers extra-low windows for better visibility of the path ahead, aluminum body panels to keep the center of gravity low, a cassette tape of off-roading tips, and a host of other features designed to keep you going after the road ends. And that, after all, is what sport-utilities are about.

Jim Treece

Electronics

RECHARGERS THAT DON'T TAKE ALL DAY

Some of life's frustrating moments occur when you find yourself powerless—that is, you start to play a portable radio or run a laptop computer and discover the batteries are dead. One solution is to keep spare alkaline batteries handy. But Eveready and others are pushing rechargeable nickel-cadmium batteries as a better idea—especially because of new technology that dramatically cuts recharging time.

Rechargeable batteries have been around since the mid-1970s. But until recently, it took at least 14 hours to pour energy from a wall socket into the popular AA and AAA batteries that power portable cassette players, toys, and many other devices. Now, Panasonic's new \$10 Slim Charger needs just six hours, and Eveready's \$15 charger



NOW, BATTERIES CAN BE READY TO GO AGAIN IN THREE TO SIX HOURS

takes just three. Eventually, they could be even faster. "The industry has the technology to cut the time to 15 minutes," says Panasonic marketing manager Dan Halaburda.

It makes economic sense to buy an inexpensive charger and a few ni-cads for as little as \$2 each—rather than

countless \$1 alkaline batteries. Because a ni-cad can be recharged as many as 1,000 times, each can provide the same hours of power as 1,000 alkaline batteries. One drawback: Ni-cads don't work with devices that use graphics, such as electronic games.

If you need just enough

power to take a few photos, the new chargers can replenish several batteries an hour or so. Studies shown that a ni-cad given a partial charge may undergo a "memory effect" and accept only a partial charge thereafter. But technicians say that's not likely to happen unless the battery is down repeatedly to empty the same point.

HOW MUCH JUICE? Rechargeables lose about 1% of energy a day—even if they're not used. Also, instead of growing weaker with use, ni-cads release the same amount of power consistently, then die. How can you know much juice a battery has? With smaller batteries, you can't. But Sony engineers came up with an answer: rechargeable camcorder batteries. A new \$130 model boasts a built-in microprocessor and five tiny green lights. Press a button, and if all lights glow, the battery is fully charged; four lights, 80% charged; and so on. When power hits 10%, the lights flash to show it's time to charge.

Don L.

Are you convinced that a certain region of the country is poised for a rebound? Or perhaps you like to invest in local companies. If so, consider regional mutual funds, an offbeat category of funds that invest in companies headquartered near each other.

Regional funds are risky, since their investments are less diversified geographically than other mutual fund portfolios. And regions such as the Sunbelt are notorious for their boom-and-bust cycles. Yet a few winning funds have beaten the market by concentrating on relatively healthy regions.

FAMILIAR TURF. "The best of these funds are managed by smaller financial firms that know the local economy better than someone 1,000 miles away," says Don Phillips, editor of Morningstar's *Mutual Fund Values*.

Smart Money

THESE MUTUAL FUNDS INVEST CLOSE TO HOME

Take one of Phillips' favorites, the IAI Regional Fund (800 927-3863). It invests 80% of its assets in companies based in Minnesota, Wisconsin, Iowa, Nebraska, Montana, and the Dakotas—an area spared the brunt of the recession. Morningstar gives the Minneapolis-based fund, run by Investment Advisors, its top rating of five stars.

The \$348 million fund's largest holdings are Sci-Med Life Systems, Medtronic, and United Health Care, health care companies in the Twin Cities area. Fund manager Bing

Carlin's edge in picking stocks: "He grew up and went to school with the top executives at many of these companies," says Phillips.

Composite Northwest 50 (800 543-8072) boasts four stars from Morningstar, but

this \$67 million fund is managed differently. The fund manager invests in companies in Alaska, Idaho, Montana, Oregon, and Washington based on their statistical weight in a 50-stock regional index. After taking a hit when the logging industry turned down, it bounced back with a midyear 1991 gain of 27.4%.

If you think the oil patch is about to make a comeback, look into the tiny, two-star, \$15 million Fund of the Southwest (800 262-6663).

Like the Midwest? The four-star Way Hummer Growth Fund (800 621-4477). You won't find Fidelity or Merrill Lynch offering a choice in this quirky group of approximately 10 funds. But you can find a well-managed mutual fund that suits your geographic fancy. Leah N. Sp

REGIONAL PICKINGS

	Total return	
	First-half 1991	Three-year average
COMPOSITE NORTHWEST 50	27.46%	20.28%
FUND OF THE SOUTHWEST	19.13	14.50
IAI REGIONAL	17.45	16.49
SOUTHEASTERN GROWTH	26.22	9.02
S&P 500 INDEX	14.27	14.67

DATA: MORNINGSTAR INC

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t a significant reference to a company. Most
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- ☐ Painkillers that make your headache worse

- ☐ Costs not covered by health insurance contract can be covered if you know the ropes
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- ☐ Quick look at sticker price plus simple arithmetic reveals minimum figure car dealer will accept

Two famous cold remedies that make you sicker if taken together

- ☐ Outwit mugger in self-service elevator
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- ☐ Stop a headache by pressing secret spot on arm
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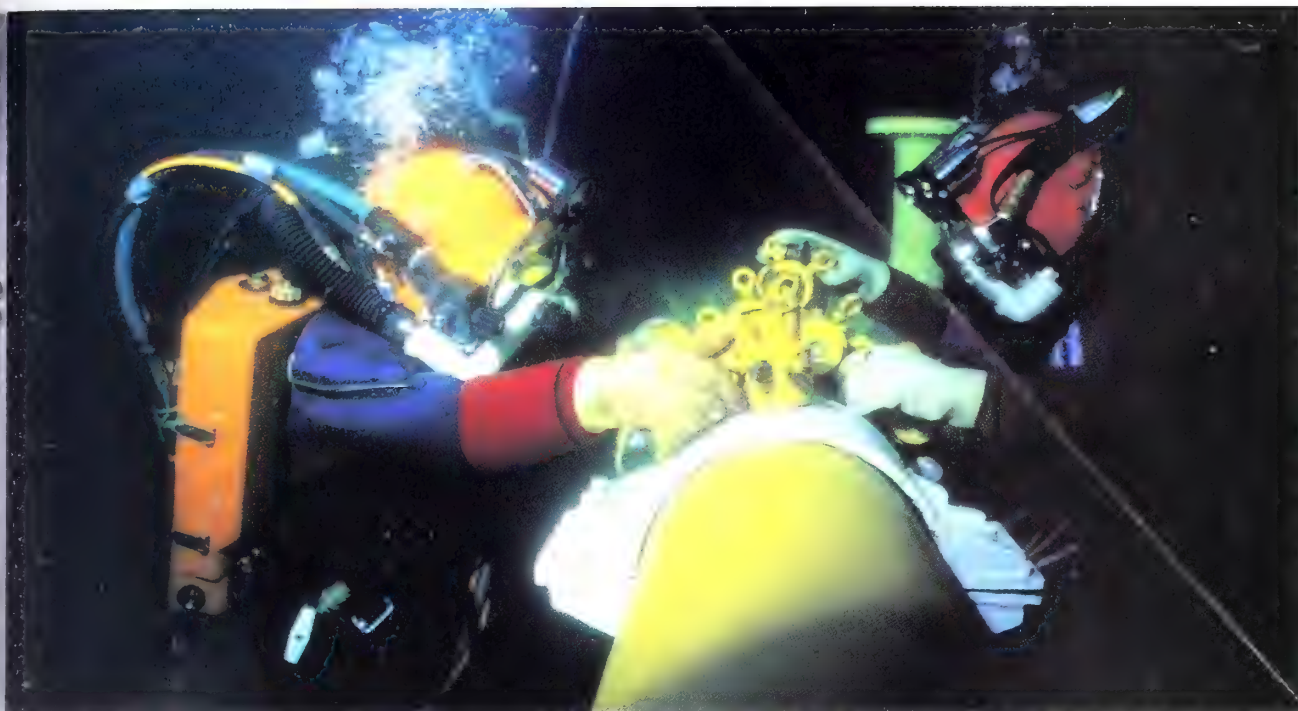
See what you have been missing

What doctors and hospitals don't tell you. What the IRS doesn't want you to know. What brokerage houses don't tell you...How to distinguish the facts from the hype in health foods, computers, pension plans...How to pick the right wines, the right exercises, the right stereo system, the right credit card.



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the four-star Wall Street Journal Hummer Growth Fund (800 621-4477). You won't find Fidelity or Merrill Lynch offering a choice in this quirky group of approximate 10 funds. But you may find a well-managed mutual fund that will suit your geographic fancy. Leah N. Spi



Comex Divers connecting a pipeline at a depth of 1,700 feet.

At a record 1,700 feet deep, the Rolex Sea-Dweller is still in its element.

The Comex aquanauts have forced forward the frontiers of the impossible. Diving from Marseilles, France, a six-man team spent eight days performing complex underwater tasks at the unprecedented depth of 1,700 ft.

Hydraliox, a combination of hydrogen, helium and oxygen, is a scientifically formulated breathing mixture that made it possible for them to live and operate at such depths.

The Comex operation is a world record, comparable in its own way to man's first moon landing. It has created huge possibilities for future research and exploration.

At such astonishing depths, with pressures of 757 lbs. per sq. in., divers must depend on something more than mere watch. They need a veritable measuring instrument: the Rolex Oyster Perpetual Sea-Dweller.

Like the Comex divers, the Sea-Dweller is strong and reliable. In addition to being pressure-proof down to 4,000 ft., it has a patented

Rolex helium escape valve to allow the expanding gases within the Oyster case to be released during ascent so that the timepiece does not experience explosive decompression.

Divers still have another 2,300 feet to descend before they rival this rugged Rolex. But then, even the most-skilled divers are always in an alien element. The Sea-Dweller is not.



ROLEX



Rolex Sea-Dweller in stainless steel with matching fliplock Oyster bracelet.



Business Week
August 19

WHY AMERICAN EXPRESS WOODED WARREN E

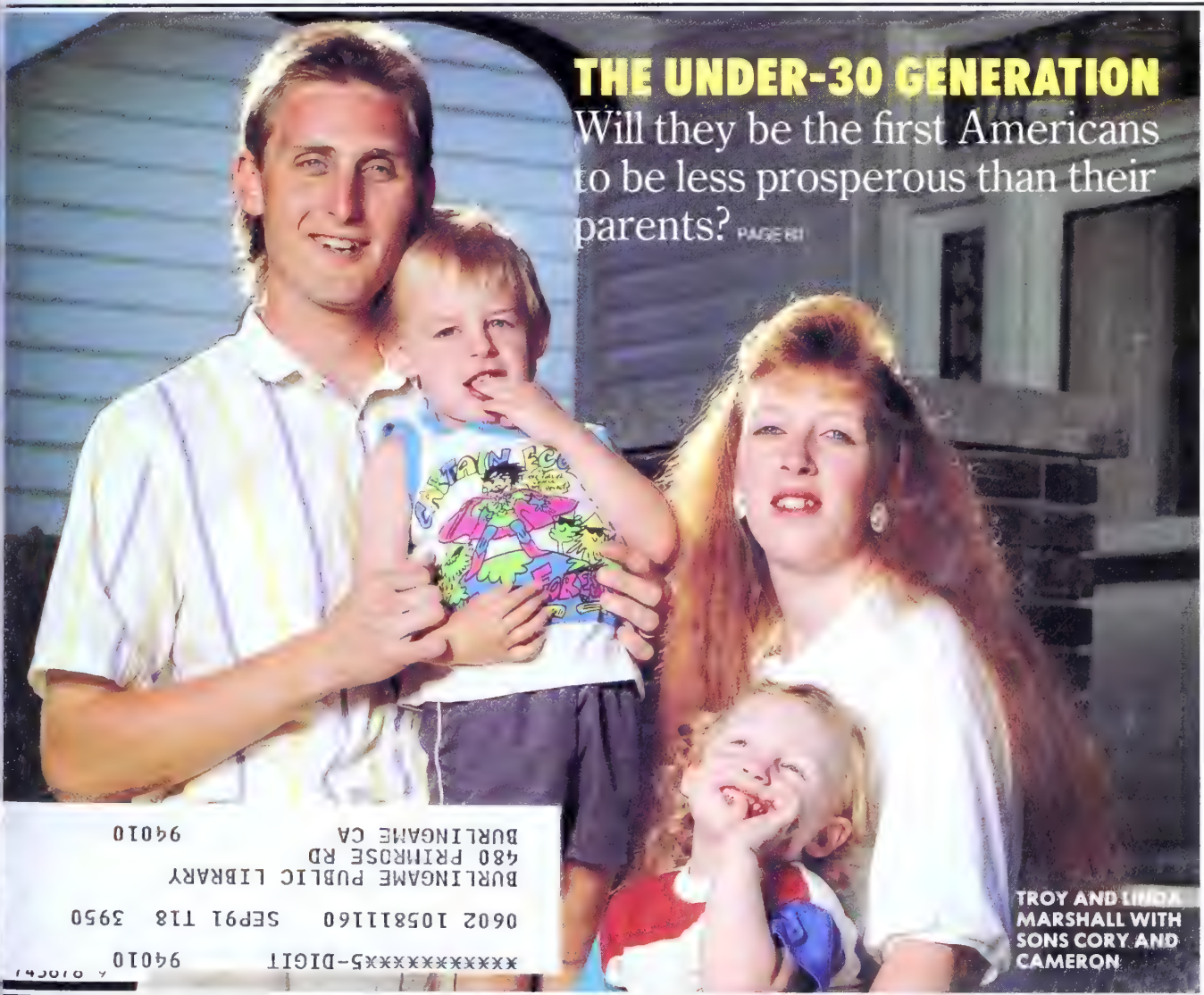
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THE UNDER-30 GENERATION

Will they be the first Americans to be less prosperous than their parents? PAGE 81

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- Digital Cellular Communications
- Mobile Communications
- Packet Switching

COMMERCIAL AVIATION

- Flight Simulators
- Landing Aid Radar
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INFORMATION MANAGEMENT SYSTEMS

- Large-Scale Integrated Systems
- Software Development
- Database Management

TRANSPORTATION SYSTEMS

- Automotive
- Traffic Management
- Rail Transportation
- Maritime Management
- Air Traffic Control
- Airport Integration

ENTERTAINMENT

- Audio Products
- Projection Television Systems
- Leisure Simulation Systems

FACTORY AUTOMATION

- Machine Tool Controllers
- Character Recognition & Material Handling Systems
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TRANSPORTATION SYSTEMS

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Hughes technology. Good for business.

HUGHES



CURTIS SMITH EXPECTED A UNION JOB, BUT THERE WEREN'T ANY. NOW, HE CAN'T AFFORD TO SUPPORT HIS GIRLFRIEND AND THEIR CHILDREN

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80 YOUNG AMERICANS

No more living with your parents. No more. The high-paying manufacturing jobs are gone.

For the first time, young Americans face lower-wage nonunion jobs, part-time work, or no work. Even the college-educated need two incomes to get ahead. For the twentysomething generation, it's a struggle to survive.

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The cruise line wants acquisitions

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DEALS, DEALS, DEALS

Henry Silverman presses on

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BUFFETT IS STASHING HIS CASH

The AmEx stock will pay him 11.6%

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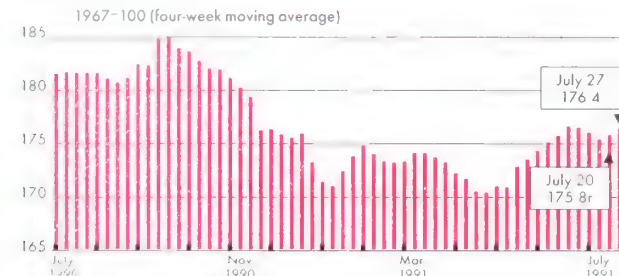
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Give young Americans a square deal
Deep-six the Missile Defense Act

BusinessWeek Index

PRODUCTION

Change from last week: 0.3%
Change from last year: -2.9%

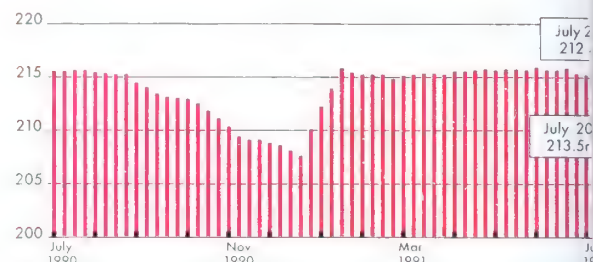


The production index increased during the week ended July 27. On a seasonally adjusted basis, electricity output fell only slightly after a large weather-related gain in the previous week. Production of autos, trucks, and lumber also dropped. Steel, coal, and paperboard output rose, while rail-freight traffic, crude-oil refining, and paper production were unchanged. Prior to calculation of the four-week moving average, the index fell to 178, from 179.4.

BW production index copyright 1991 by McGraw-Hill Inc.

LEADING

Change from last week: -0.5%
Change from last year: -1.5%



The leading index declined during the week ended July 27. Most of the decrease was caused by a sharp drop in the prices of industrial materials and a jump in the number of business failures. The growth rates for M2 and real estate loans slowed, and stock prices were lower. Bond yields fell slightly in the last week. Before calculation of the four-week moving average, the index dropped to 210.1, from 212 in the previous week.

Leading index copyright 1991 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (8/3) thous. of net tons	1,625	1,668#	-12.4
AUTOS (8/3) units	79,343	79,416#	-17.4
TRUCKS (8/3) units	41,735	58,230#	-40.8
ELECTRIC POWER (8/3) millions of kilowatt-hours	63,847	67,382#	1.5
CRUDE-OIL REFINING (8/3) thous. of bbl./day	13,587	13,842#	-6.0
COAL (7/27) thous. of net tons	20,036#	19,372	-2.2
PAPERBOARD (7/27) thous. of tons	804.6#	798.1r	6.8
PAPER (7/27) thous. of tons	752.0#	742.0r	-0.3
LUMBER (7/27) millions of ft.	528.0#	556.9	8.3
RAIL FREIGHT (7/27) billions of ton-miles	19.6#	19.4	-5.3

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Paper Institute, WWPAA, SFPA, Association of American Railroads.

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (8/7)	136	138	150
GERMAN MARK (8/7)	1.71	1.74	1.60
BRITISH POUND (8/7)	1.71	1.69	1.87
FRENCH FRANC (8/7)	5.83	5.93	5.36
CANADIAN DOLLAR (8/7)	1.15	1.15	1.15
SWISS FRANC (8/7)	1.50	1.52	1.35
MEXICAN PESO (8/7) ¹	3,024	3,022	2,882

Sources: Major New York banks. Currencies expressed in units per U. S. dollar, except for British pound expressed in dollars.

PRICES

	Latest week	Week ago	% Change year ago
GOLD (8/7) \$/troy oz.	356.800	362.850	-7.3
STEEL SCRAP (8/6) #1 heavy, \$/ton	94.00	90.50	-20.3
FOODSTUFFS (8/5) index, 1967=100	205.2	205.8	-5.0
COPPER (8/3) c/lb.	105.1	103.6	-20.3
ALUMINUM (8/3) c/lb.	58.5	58.9	-26.9
WHEAT (8/3) #2 hard, \$/bu.	3.08	2.99	6.2
COTTON (8/3) strict low middling 1-1/16 in., c/lb.	69.12	70.00	-12.8

Sources: London Wednesday final setting, Chicago market, Commodity Research Bureau, Metals Week, Kansas City market, Memphis market.

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (8/2) S&P 500	386.39	380.57	
CORPORATE BOND YIELD, Aaa (8/2)	8.93%	8.97%	
INDUSTRIAL MATERIALS PRICES (8/2)	96.4	96.7	
BUSINESS FAILURES (7/26)	376	271	
REAL ESTATE LOANS (7/24) billions	\$399.8	\$400.2	
MONEY SUPPLY, M2 (7/22) billions	\$3,398.4	\$3,397.6r	
INITIAL CLAIMS, UNEMPLOYMENT (7/20) thous	404	425	

Sources: Standard & Poor's, Moody's, Journal of Commerce (index: 1980=100), Dun & Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. CIBCR seasonal just data on business failures and real estate loans.

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
EMPLOYMENT, CIVILIAN (July) millions	116.7	116.9	-0.1
UNEMPLOYMENT RATE, CIVILIAN (July)	6.8%	7.0%	2.6
PURCHASING MANAGERS' INDEX (July)	51.8%	50.9%	8.8
CONSTR. SPENDING (June) annual rate, billions	\$400.3	\$399.2r	-11.1

Sources: BLS, National Association of Purchasing Management, Census Bureau

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (7/22)	\$860.2	\$857.7r	
BANKS' BUSINESS LOANS (7/24)	302.6	304.1r	-1.1
FREE RESERVES (7/24)	464r	290r	31.1
NONFINANCIAL COMMERCIAL PAPER (7/24)	145.0	147.5	

Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed for two-week period in millions)

MONEY MARKET RATES

	Latest week	Week ago	% Change year ago
FEDERAL FUNDS (8/6)	5.70%	5.75%	8.0
PRIME (8/7)	8.50	8.50	10.0
COMMERCIAL PAPER 3-MONTH (8/6)	5.84	5.96	7.7
CERTIFICATES OF DEPOSIT 3-MONTH (8/7)	5.64	5.92	7.8
EURODOLLAR 3-MONTH (8/3)	5.91	5.98	7.8

Sources: Federal Reserve Board, First Boston

#Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

IF WE ALL AGED
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THE WORLD WOULD BE
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Some say the secret to the popularity of Ballantine's Finest Scotch is its artful blend of 42 single malt whiskies. Others proclaim the virtues of water, peat or heather, traces of which can be detected in every sip. But all discussions about Scotch must ultimately turn to the oak barrels in which it matures.

Newly distilled single malt Scotch enters the barrel naked, virtually clear, fiery in its potency, but somewhat lacking in manners. Over the years it acquires a golden hue, drawn from the wood itself. Air penetrates the porous surface, whispering hints of the outside world to the budding whisky inside. In turn, evaporation imparts a subtle sweetness to the surrounding air.

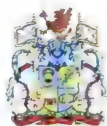


When the whisky emerges from its long metamorphosis, it has mellowed considerably. Tempered with soft Scottish water and merged into the Ballantine's Finest blend, each of the single malts confidently introduces itself to your glass, proud of its origin, asserting its flavor with the firm handshake of individual Scotch character.

Then a softer side to Ballantine's is revealed, a sentimental quality that blooms on the palate like a flower unveiling hidden color. The finish is gentle but firm, dignified and noble.

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CHEAP CAPITAL? DON'T COUNT ON IT

The articles "The playing field is level—so play" (Editorials, Aug. 5) and "The U.S. has a new weapon: Low-cost capital" (Economics, July 29) may be premature.

To be sure, interest rates have declined and stock/price earnings have increased, but these trends may be recession-induced and may disappear with recovery. The latter interpretation is bolstered by the fact that the fundamental causes of high long-run U.S. capital costs have not been corrected. These fundamental causes include our ultralow national saving rate and ultrahigh taxation of the income from productive investment.

Since the huge federal deficit is a major cause of the low national saving rate, a conceptually simple but politically difficult solution suggests itself. Enact a broad-based consumption tax (every other major industrialized nation already has one) and use part of the proceeds for deficit reduction and part to directly lower taxes on the income from productive investment.

Raising the saving rate would indirectly cut capital costs by lowering interest rates. Cutting the taxes on investment income would directly reduce capital costs.

Competitiveness considerations aside, the resulting stimulus to productive investment—so lagging in recent years—would help restore strong growth to what has been a very sluggish rise in U.S. living standards since the mid-1970s.

Charles E. Walker

Chairman

Charles E. Walker Associates Inc.

Washington

YOU WON'T FIND ANY PADDING IN INSURERS' BOOKS

I'd like to take issue with your commentary "Letting the air out of insurers' overblown assets" (Finance, July 8). As you know, accounting principles require that equity-based securities be carried on an insurer's books at market val-

ue, debt instruments at amortized value, and certain other assets—including real estate—at the lesser of cost or current value.

Switching to a current-market-value methodology, as the author suggests, is an interesting idea as it could provide a more accurate assessment of a firm's liquidation value.

Unfortunately, a firm's liquidation value is generally of little concern. Both generally accepted accounting principles and statutory accounting principles are designed, for good reason, to value a firm as an ongoing concern rather than as one about to be liquidated.

Further, the National Association of Insurance Commissioners' prescribed annual statement forms already provide an accurate assessment of an insurer's financial strength.

It cannot be argued that the insurance industry is immune to insolvencies. Recent history bares this truth well. Just like many banks and savings and loan associations, poor management or investment decisions have jeopardized the financial soundness of some insurers. Nonetheless, insurance companies as a whole have the strongest balance sheets in the financial industry, and their strength is measured conservatively, accurately, fairly, and in the public's interest—points that the commentary failed to mention.

Charles D. Eckerson

Regional Accounting &

Controls Manager

Nationwide Mutual Insurance Co.

Raleigh, N.C.

MUTUAL BENEFIT'S SLIDE ISN'T EX-CEO KATES'S FAULT

In the otherwise accurate article "Panicky policyholders have insurers trembling" (Finance, July 29), on the problems facing the life-insurance industry, BUSINESS WEEK does Mutual Benefit Life Insurance's former chief executive, Henry Kates, an enormous disservice.

By not listing the chronology of Kates's employment at Mutual Benefit, the article implies that he was the individual responsible for Mutual Benefit's heavy reliance on real estate investments, and indeed, that he also super-

BUSINESS WEEK
AUGUST 19, 1991 ***3227
ISSN 0007-7135



Published weekly, except for one issue in January, by McGraw-Hill, Inc. Founder James H. McGraw (1860-1948). Executive, Editorial, Circulation, and Advertising Offices: McGraw-Hill Building, 1221 Avenue of the Americas, New York, N.Y. 10020. Telephone: (212) 512-2000 Domestic Telex: 127960; International Telex: 232365; Cable: McGraw-Hill New York; TWX: 710-381-4879. U.S. subscription rate \$44.95 per year; 2 years, \$74.95; 3 years, \$99.95. Single copies, \$2. Write for rates in other countries. Business Week Subscriber Services: 1-800-635-1200

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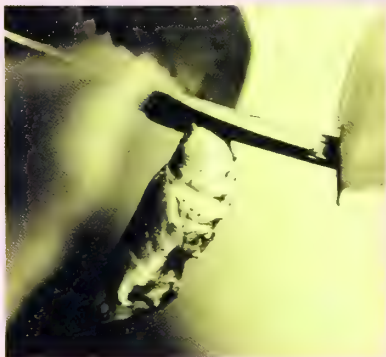
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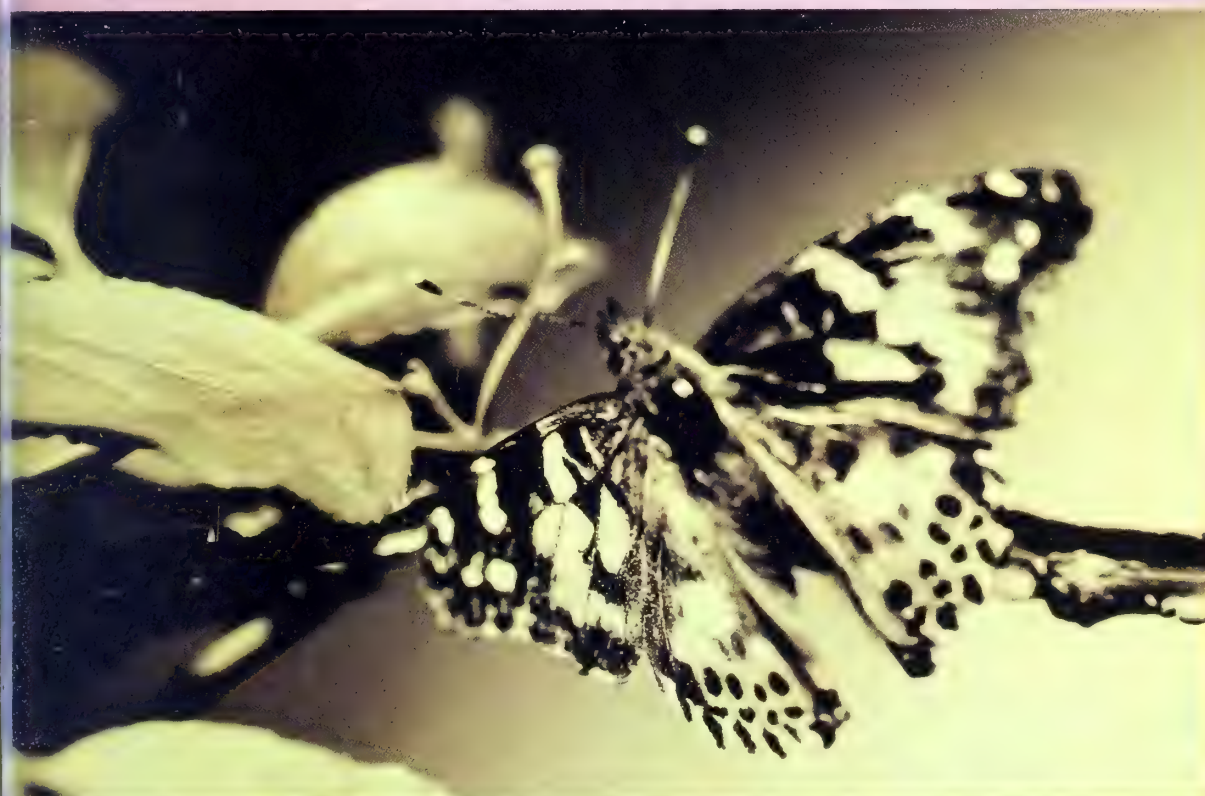
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Readers Report

vised the company's rapid expansion into "GICs and other retirement products."

In fact, Hank Kates became the CEO of Mutual Benefit long after these strategic decisions had been made by his predecessor and the company's former chief investment officer.

It is to Kates's credit that he addressed the problems in Mutual Benefit's real estate portfolio as they developed, and his leadership displayed both a shrewd understanding of the threat facing Mutual Benefit and the courage to tell the truth about it to both the rating agencies and the various regulators involved.

John P. Mascotte
Chairman & Chief Executive Officer
Continental Corp.
New York

PLENTY OF INCENTIVES FOR ESOPs REMAIN

Regarding your story "The real strengths of employee ownership" (Editorials, July 15), the 1989 tax law did eliminate one tax incentive for employee stock-ownership plans that was costly to the taxpayer but had relatively little impact on the number of new plans set up.

Most professionals in this field would have rated it only as the fourth or fifth most important ESOP incentive. So the basic tax structure for ESOPs remains intact.

Corey Rosen
Executive Director
National Center for
Employee Ownership
Oakland, Calif.

NO ONE SHOULD EXPECT ISRAEL TO TRUST A TERRORIST

Your story "Peaceful straws in the Mideast wind" (International Outlook, July 29) is remarkably naive about the latest maneuvering in Arab-Israeli peace prospects.

Syria's President Hafez al-Assad has been a staunch supporter of terrorism, with responsibility for the bombing of the U.S. Marine barracks in Lebanon and the horrific Pan Am 103 terrorist act. He has committed mass murder and atrocities in Syria itself and holds nearly 5,000 Syrian Jews hostage.

To suggest that this leopard has changed his spots and Israel should simply trust Assad is unfortunate. It is furthermore incredibly sad to hint that hu-

manitarian loan guarantees would be held hostage to anything that might be done with disfavor in the Administration's eyes.

William E. Rapf
Executive Director
Institute for Public Affairs
Union of Orthodox Jewish
Congregations of America
New York

THIS CONSULTING SERVICE IS AVAILABLE NOW, NOT LATER

We were delighted you mentioned Meritus Consulting Services, a joint venture between IBM and Cook & Lybrand, in your recent article. "Is it time to junk the way you use computers?" (Information Processing, July 22).

Unfortunately, your article states that we will begin selling re-engineering services next June. In fact, Meritus Consulting is currently offering these services, with outstanding results for customers.

E. Clark Griener
President
Meritus Consulting Services
Greenwich, Conn.



W MANY \$60,000 CADILLACS LL THE JAPANESE BUY?

ittle wonder we can't sell cars in Japan if Cadillacs are going for a mere \$60,000, while at the same time rebates are being offered on Japanese cars sold in the U.S. ("What's this? American cars gaining in Japan?," Industries, 7/22).

Meanwhile, millions of Japanese cars are literally being dumped in the U.S. at prices I suspect are equal to or lower than prices paid in Japan for the same cars. And gosh, isn't it wonderful that we sold top our record sales of 16,709 units in 1979. We even sold 18,000 or 20,000 units a year.

Harold E. Reed
Ledyard, Conn.

THE BANKS—DON'T THEM RUN AMOK

your editorial "Banking reform: Just a minute" (July 15), you arrived at the conclusion that banks should be able to get into other states and should be able to enter other businesses. I take the opposite approach. The sickness of the banking industry must be fixed before the federal government al-

CORRECTIONS & CLARIFICATIONS

In the story "Do more babies mean fewer working women?" (Labor, Aug. 5), we incorrectly identified Ann McPherson and her husband. She is former office manager of a small company in Denver; he is a financial analyst with Martin Marietta Corp.

In a table (The Global 1000, July 15), we misstated the price-earnings ratio and return on equity for Enron Corp. The correct numbers: PE, 16; ROE, 11.4.

In the story "The long and winding road to BCCI's dead end" (Finance, July 22), we said Clark M. Clifford, chairman of First American Bankshares Inc., and other investors bought shares in the bank's stock with BCCI loans that were never repaid. The loans were repaid in 1988.

allows the industry to get bigger so that we can have bigger failures. Almost no bank failures took place between 1933 and 1983.

What did we do to undo the stability of our banking industry, created during the Depression? If you know the answer, then you know how to

fix the banking industry; but if not, then you really don't understand.

George Lasky
Dallas

INSURERS ARE RATED A+ to C- —AND THEN SOME

I am sure your sidebar "The rating game: When A+ equals C-" (Cover Story, Aug. 5) helped your readers better understand the different scales used by raters of insurance companies.

You omitted, however, in your table's lowest rating category, "Nonviable or about to be," the reference to our NA-7 (Below Minimum Standards) classification assigned to companies that do not qualify for our minimum rating of C-. A. M. Best's analysis of 1,525 life/health insurers assigned a rating of A+ to C- to 765 companies, an additional 46 were rated NA-7, and the remaining 530 were not eligible for a rating.

Arthur Snyder, Chairman
A. M. Best Co.
Oldwick, N. J.

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RIVETHEAD: TALES FROM THE ASSEMBLY LINE

By Ben Hamper

Warner • 234pp • \$19.95

A SHOP RAT LAYS IT ON THE LINE

Car, windshield, Car, windshield. Drudgery piled atop drudgery. Cigarette to cigarette. Decades rolling through the rafters, bones turning to dust, stubborn clocks gagging down flesh, another windshield, another cigarette, wars blinking on and off, thunderstorms muttering the alphabet, crows on power lines asleep or dead, that mechanical octopus squirming... I wanted to shout at my father 'Do something else!' Do something else or come home with us or flee to the nearest watering hole. DO SOMETHING ELSE! Car, windshield...."

So writes former auto worker Ben Hamper in his angry yet comical *Rivethead: Tales from the Assembly Line*, a powerful book that often reads like the biting poetry of Charles Bukowski, laureate of Los Angeles lowlife. Hamper, who followed Dad's footsteps despite his loathing

for the line, was a riveter at General Motors Corp.'s Truck & Bus Div. plant in Flint, Mich., for 11 years. A nervous breakdown in 1988 compelled him to give up his cherished nightmare of someday winning a GM 30-year pin. But along the way, he developed a talent for writing and began publishing his meditations on factory life. In time, his "Rivethead" column, from which parts of the book are drawn, appeared in the *Detroit Free Press* and *Mother Jones* magazine.

Rivethead is far more than one man's musings on life in an auto plant. It is about class, the working class, and the lives led by the American men and women who manufacture the things we buy. It is about people who sweat for their pay. These folks, Hamper says, still toil in unsafe factories for companies that don't care—companies that, despite their prattle

about employee participation, often treat workers like children.

Hamper traces his rocky journey from underachieving, abused child to assembly line worker. Not just his father, but great-grandfather, three grandfathers and two uncles had been auto workers. Everything prepared him for the assembly line—even grade school. "The education-through-intimidation technique favored there was not unlike the jarhead mentality of the General Motors f lords," he writes. "Our fathers' overseers were brutes with clipboards, sideburns and tangled rhetoric. Our overseers, sisters of St. Luke's, were brutes with clipboards, sideburns, and tangled rosaries."

Hamper rebelled briefly, doing dishwashing while working as a housepainter. Then, married and a father within months of high school graduation, he soon embraced his "birthright" at the GM plant. Just 10 months later, he writes, another worker began to break down under the slow-motion injustice of the time clock. The man's emotional collapse was complete when he took a blowtorch to a machine he had befriended. "Roy insisted," Hamper reports, "that the mouse was mousing the way he performed the job."

Hamper's humor, which undoubtedly

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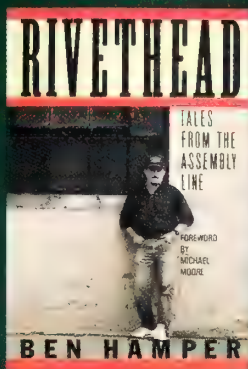


The HP PaintJet and PaintWriter.

ed him survive, keeps
gs lively. The book is
pered with wisecracks.
t is "a town whose col-
ive bowling average is
times higher than the
of its inhabitants." For-
GM Chairman Roger B.
th is "perhaps the only
in the entire Western
nisphere to possess
million freckles and
absolutely no sense of
or whatsoever." Which
t deter Hamper from
ging Smith to share an
ing of bowling.

that sounds like the
of the movie *Roger &*
in which director Mil-
el Moore trails Smith in an attempt to
uss the impact of GM layoffs on Flint,
e's probably more than coincidence at
k. It was during one of three layoffs
Hamper began writing, starting with
ic reviews for the underground *Flint*
ce, founded by Moore. That gig led to
"Rivethead" column. In fact, Hamper
eared briefly in Moore's 1989 film: He's
guy shooting hoops at the mental
th clinic—the one who, fearing anoth-
ayoff, had a panic attack on the line,
had a breakdown while listening to

Boredom, booze,
breakdowns, grisly
accidents—yet
Hamper finds humor
in life at the plant



toonlike character. Instead,
"Howie sightings" became
a joke to relieve boredom:
"The workers would
scream and holler and
jump up and down on their
workbenches whenever
Howie drifted by." Later,
they took to pelting him
with rivets. The book also
details the social problems
of line workers—usually
too much booze—and ex-
plores life during layoffs.

Like his column, which
Hamper says drove GM to
spy on him, this book won't
please everyone. Hamper's
prose is laced with obscen-
ities, and the fainthearted

the Beach Boys sing *Wouldn't It Be Nice*?

Most of *Rivethead* focuses on the in-
dignities of life as a shop rat. There's the
message board that flashes "Squeezing
Rivets Is Fun!" There are shop foremen
who allegedly refuse to stop the line to aid
injured workers. And there's Howie Ma-
kem, the plant mascot—a guy dressed as a
cat and wearing a long, red cape embla-
zoned with a "Q" for quality. Some white-
collar dunce, Hamper figures, probably
thought the proles could relate to a car-

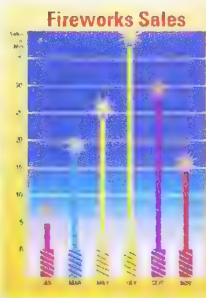
may grow queasy when Hamper's buddies
lose fingers or slash limbs while using
dangerous machinery.

By plumbing his life and the lives of his
co-workers, Hamper reveals in ugly detail
the two-tier society that persists despite
comforting rhetoric about opportunity and
bootstrap success. It's a world where
workers suffer and cope through drink or
madness. Not pretty. But compelling.

BY KEVIN KELLY

Chicago Correspondent Kelly once worked
the night shift in a plastic-bag factory.

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CAN JAPAN'S COZY SYSTEM COME TO TERMS WITH CHANGE?

BY ALAN S. BLINDER



Japan's long-term, cooperative business practices are a success. But foreigners pose a threat to their exclusionary ways, and may even start raiding some of the local talent

ALAN S. BLINDER IS THE GORDON S. RENTSCHLER MEMORIAL PROFESSOR OF ECONOMICS AT PRINCETON AND THE AUTHOR OF *HARD HEADS, SOFT HEARTS*

Like many of the things you buy, this column was made in Japan, where I am spending some time trying to unravel the mysteries of the Japanese economy. Since Japanese scholars who have devoted years to this task still find themselves somewhat in the dark, I do not expect to figure the whole thing out in two weeks. Nonetheless, as I travel around sultry Tokyo talking to economists, business executives, and government officials, two terms keep cropping up. These expressions will not surprise you: "long-term" and "cooperation." Whether the subject is employment practices, linkages among business firms, or the role of government in the economy, the essence of the Japanese system seems to be long-term, cooperative relations.

It's true that workers and companies stick together much longer in Japan than in the U.S. Practically no one gets fired. And labor-management relations are, by our standards, astonishingly cooperative. In the U.S. and Europe, the "us vs. them" attitude often impairs industrial productivity. In Japan, it is just "us."

Much the same can be said about relations between companies doing business with one another. Japanese companies tend to remain more loyal to their suppliers, banks, and distributors than is typical in the U.S. These relationships—some would say cozy relationships—are not formalized in written contracts but are based on mutual trust built on long-term associations.

BOTH/NEITHER. The same two words come up in discussing relations between government and business. Why is the business-government relationship, which is so adversarial in the U.S., so amazingly cooperative in Japan? One main reason is that Japan's big companies know they will encounter the country's powerful ministries time and time again. There is not much incentive to stonewall, ignore, or double-cross the other guy (yes, they are all guys) when you know you will be dealing with him often throughout your career. Besides, businesses believe that the ministries are there to help. Does that mean that government controls business or that business controls government? Actually, it's both—and neither. A Japanese businessman will either comply with a bureaucrat's wishes or humor him; outright defiance is bad form—and unwise.

Long-term, cooperative behavior holds some evident rewards. It enables Japanese workers, companies, and ministries to invest in physical capital, skill formation, and human relationships much more than their U.S. counterparts. And it increases economic efficiency by sharply delimiting incentives to engage in

opportunistic behavior for short-term gain. This much is obvious. But when we think more deeply about these matters, certain problems arise.

There is such a thing, for instance, as sticking together too long. Basic economics teaches that the invisible hand works best only when labor and other resources are free to move. Indeed, during the 1980s one popular diagnosis of "Eurosclerosis" was that Europe suffered from locking resources in place, while the U.S. let them move. In Japan, however, mobility hardly exists, and manufacturers tend to use the same suppliers and distributors for years, and it is far from clear that even capital flows freely to maximize return. Yet, somehow, the Japanese have done very nicely, thank you. Could it be that the virtues of mobility have been oversold?

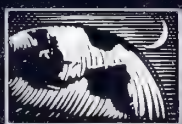
MEMBERS ONLY. A second puzzle is how long-term, cooperative arrangements are maintained in the face of what appear to be other powerful incentives to break them. Consider the gentlemen's agreement not to raid other firms for talent. Suppose Yoshio is a talented executive at Sumitomo Bank, but his career path is blocked by Kazuo, who has been with the bank a year longer. In the U.S., Yoshio would probably find a new job. But in Japan the doors at other banks are shut. Why? On the surface, it would appear that Yoshio, by competing bank, and the Japanese economy would all benefit from mobility. But Japanese mores and business practices block the way. Somehow the lid is kept on.

There's the rub. Foreigners pose two kinds of problems for Japan's long-term, cooperative system. First, while long-term relationships may be efficient, they are also inevitably exclusionary. So foreign businesses entering Japanese markets complain that they cannot gain admission to the club. Japan must therefore choose between modifying its eminently successful system or seeing itself embroiled in endless trade disputes.

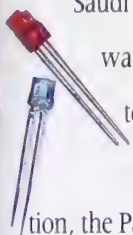
The second problem pertains to the potential conflict between imported self-interest and cooperation. If, for example, an American bank opens up in Tokyo, it will be only too happy to hire the talented Yoshio. Once there are enough foreign banks in the Japanese market, the boat will be heavily rocked.

The Japanese see change coming; you hear them say so everywhere. The pressure for change comes partly from the outside world and partly from the younger generation, who finds the status quo somewhat stultifying. Japan's leaders are understandably concerned. What happens, they wonder, when a system that is not broken gets fixed?

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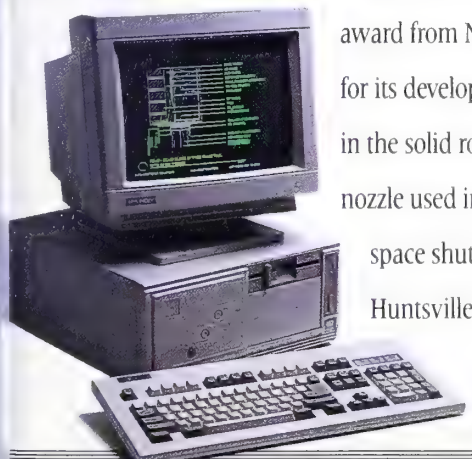
As Iraq aimed its Scud missiles at Israel and Saudi Arabia during the Gulf War, the world watched America's Patriot missiles vault toward them, destroying them time after time. After the first successful interception, the Patriot became a household word for many Americans. But most people didn't know that Alabama played a major role in its creation.

The concept for the anti-aircraft guided missile was born at Redstone Arsenal near Huntsville. Alabama companies and their workers made important contributions to the creation of the Patriot missile—from

systems engineering and software support to production of the rocket motor. Technical schools in Alabama continue to produce a labor base well-suited to high-tech manufacturing. Together, Alabama technology

and labor helped win Operation Desert Storm. Defense isn't the only industry to benefit from Alabama's technological capabilities. QMS, Inc. in Mobile is a world leader in the development, manufacture, and marketing of intelligent printer systems and software. Southern Research Institute in Birmingham received an

award from NASA for its developments in the solid rocket nozzle used in the space shuttle. Huntsville's



Intergraph, which designs interactive computer graphics systems, has branch offices in 41 countries worldwide. And just outside of Montgomery a new TechnaCenter is being built to further nurture high-tech research and development. The center, with over \$5 billion in contracts,

The development of the Patriot missile, a mobile anti-aircraft system with track-via-missile guidance, was initiated in Alabama. It's considered one of the most successful weapons used in Operation Desert Storm.

will be a unique blend of university resources, state institutions, defense-related contractors, and private enterprise.

While Alabama's high-tech experience may not be as well-known as other

states', we're gaining more attention from decision-makers who visit here. JVC America, for example, established its headquarters in Tuscaloosa after seeing the research support offered by the University of Alabama

and the quality of the area's labor force. The results exceeded their expectations; within the first two years of operation, the Tuscaloosa plant was recognized as the most productive JVC plant worldwide.

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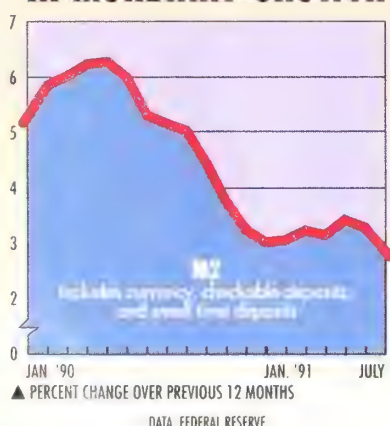
BY GENE KORETZ

WHY THE FED'S FAVORITE INDICATOR DOESN'T REFLECT THE REBOUND

Does money matter in sustaining the nascent recovery? That's the critical question posed by the unusually sluggish behavior of the money supply, which normally grows rapidly at the onset of an upswing. At last count in late July, M2, the Federal Reserve's favorite monetary aggregate, was virtually stagnant—up only 2.8% over its year-earlier level—compared with an average 12-month growth rate of 7.2% at the start of the previous five recoveries.

Although the Fed eased slightly in early August, it claims to be unperturbed. As Robert Parry, president of the Federal Reserve Bank of San Francisco, recently commented, the relation

NO SIGN OF RECOVERY IN MONETARY GROWTH



of M2 "to economic activity in the short run is highly variable." The prevailing view at the Fed seems to be that recent changes in the financial system and in investor behavior are causing monetary measures to underestimate the availability of liquidity in the economy.

The biggest factor affecting money measures is the drastic downsizing of banks and thrifts. Economist Martin Barnes of *Bank Credit Analyst* estimates that highly leveraged transactions and commercial real estate accounted for 40% of the increase in bank lending during the second half of the 1980s. The drop in loan demand associated with the purging of these excesses, he notes, implies a shrinkage of bank assets accompanied by a lessened need for deposits. The upshot has been an outflow of funds from banks into savings instruments—bond and equity funds, Treasury securi-

ties, and the like—that aren't part of the basic money supply.

Economist Robert DiClemente of Salomon Brothers Inc. describes how the Fed's shift toward ease has tended to foster this process. With the Fed funds rate down by about 30% over the past year, the money-market yield curve—the gap between short- and long-term interest rates—has steepened considerably. But the yield curve among bank deposits has flattened as banks and surviving thrifts have sought to boost profit margins by holding down the rates they're willing to pay for time deposits.

The result: Confronted with the far more attractive returns available outside the banking system, households have been moving aggressively into open-market instruments—investing more in bond funds over the past four months, for example, than they did in all of 1990. In sum, monetary growth has slowed because of portfolio shifts among individual savers.

What's more, DiClemente notes that the most liquid components of M2—currency, checkable deposits, and passbook savings accounts—have grown at a healthy 9.7% annual rate over the past six months. "Since these are the instruments that can be drawn down quickly to support a pickup in spending," he says, "the trend suggests that monetary ease has been effective."

Such arguments seem particularly compelling to a Fed that has a history of panicking in the early stages of past recoveries and stimulating too much. But the acid test will be the behavior of the economy itself. As the Fed's latest nudging of the funds rate suggests, the pressure to ease aggressively could reach a critical mass if money growth stays slow and the recovery appears to be faltering.

CEO PAY: EXORBITANT, YES —ILLOGICAL, NO

Pay levels of chief executive officers may seem unduly high at a time when ordinary workers are scrambling to make ends meet, but that doesn't mean their pay is unrelated to their companies' performance. Early results from the latest Hay Group Inc. executive compensation survey show a strong relationship between CEO annual cash compensation, particularly incentive payouts, and company profitability.

Base salaries for CEOs in 40 large industrial companies chosen at random by the management consulting firm rose an average of just 6.6% this year, and a third of the top brass received no in-

crease at all. More significantly, CEOs of companies whose profits were down 2% last year had their bonuses trimmed back by an average 19%. And those whose corporations racked up profit gains of 20% garnered average bonus hikes of 19%. The close relationship between profits and bonuses, reports Hay Group, "is apparent in almost all of the individual companies surveyed."

MANUFACTURERS ARE STILL SINGING THE BLUES

Given their industry's endemic problems, it's hardly a surprise that construction companies surveyed by D&B & Bradstreet Corp. in mid-July reported plummeting orders and little hope for an upturn in coming months. Less predictable, however, was the continuing pessimism exhibited by some 1,000 manufacturers also surveyed last month. The manufacturers reported declines in both production levels and overall new orders over the past three months and a rise in export orders. D&B says the survey suggests that "recent small improvements in manufacturing data are not sustainable."

TAX RATES ARE UP, BUT RECEIPTS ARE WAY DOWN

The pickup in economic activity that apparently began last quarter has not bolstered federal tax receipts. Indeed, economists Gert von der Linde and Richard F. Hokenson of Donaldson, Lufkin & Jenrette Securities Corp. point out that total federal revenues started exhibiting "an ominous decline" in May and June, falling 8.1% and 6.5% from their year-earlier levels. The drop occurred despite a sizable rise in tax rates that was legislated last fall.

The two economists note that individual income-tax receipts have been declining on a year-over-year basis since December and are down 1.1% for the first nine months of fiscal 1991, compared with the Administration's projection of a 5.5% increase last February. And total receipts from all sources are now running only 1.5% over fiscal 1990, an anemic rate of gain that, if maintained, will produce a \$45 billion gap between actual and originally projected levels for fiscal 1991. In fact, von der Linde and Hokenson expect the shortfall to be much larger because it has been growing steadily all year.

1956.



1965.



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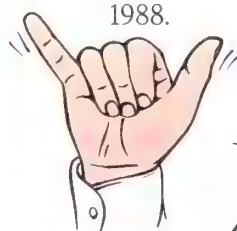
1975.



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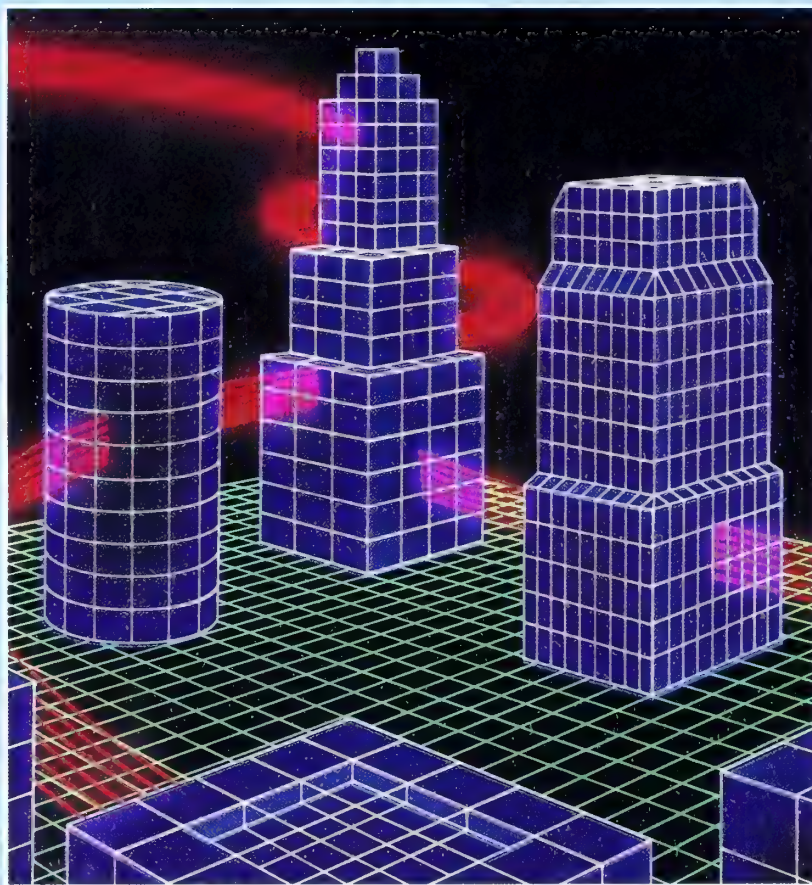
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BusinessWeek

EVEN THE FED IS GETTING NERVOUS ABOUT THIS RECOVERY

Nashington's economic reports often come and go without much impact on the outlook. But every once in a while there's a real eyepop—like the July employment report. Last month's job report looked more like an economy in recession than in recovery. The numbers not only confirm that the upturn is abating, they fuel concern that the rebound could fall out by yearend.

If that sounds like an overstatement, consider the following: In July, payrolls shrank for the second consecutive month. The workweek fell sharply, erasing gains in May and June. And weekly earnings posted the second-largest drop on record. It's not the kind of report that suggests the economy is on track to expect three months or so into a recovery.

LONG RATES TAKE A TUMBLE



The numbers clearly got the attention of the Federal Reserve Board. The Fed eased monetary policy on Aug. 6, for the first time since Apr. 30, by cutting the federal funds rate on interbank lending by a quarter point, to 5½%. The easing could lead to a lower prime rate, currently at 8.5%, but profit-starved banks may hold off until the Fed takes an even bolder

step by cutting the highly symbolic discount rate. Even though the spread between the prime and banks' cost of funds is already gaping, banks seem to be in no hurry to boost lending. Instead, their emphasis is on satisfying stricter regulators, meeting higher capital requirements, and dealing with existing bad loans. Consequently, further Fed easing may be necessary to end the credit crunch, but another rate cut will also depend upon more reports on economic growth and inflation.

After seeing the employment report, analysts had expected a cut in the federal-funds rate at the upcoming policy meeting on Aug. 20. Taking the action now only underscores the Fed's concern about the fragile state of the economy. Indeed, the Fed's own report on business conditions in each of its 12 districts, indicates that the recovery is slow and uneven.

MONEY GROWTH STILL SLAGGING

Worries about weak money growth also prompted the Fed's action. The central bank's favorite money measure, M2, had been expected to rise for the week ended

July 22, but it fell a steep \$5.5 billion. The pace of M2 growth has dropped to an annual rate of only 2.7% from the Fed's fourth-quarter base, barely

above the bottom of the central bank's 2.5% to 6.5% target range. The July employment report heightens concern that exceptionally weak money growth for the early stages of a recovery may be inconsistent with the Fed's desire for a sustainable upturn.

The weak job data also put the kibosh on inflation fears. So much so, that the bond market rallied after the Fed's move. Past easings often have pushed long-term interest rates higher on bond traders' fears that easier money might fuel faster price growth.

But this time, long-term rates declined, even with the upward pressure from the Treasury Dept.'s record \$38 billion quarterly refunding. The rate on 30-year Treasury bonds, for example, fell to 8.17% on Aug. 6. Only two weeks earlier, it stood at just under 8.5% (chart).

LABOR MARKETS LOOK SHAKY

Lower long-term rates will eventually help the economy's credit-sensitive sectors, but for now, the labor markets make it clear that the recovery is off to a rocky start. Nonfarm businesses let go 51,000 workers in July, following a cut of 21,000 in June. Employment had jumped by 151,000 in May, so it remains only about 80,000 jobs above the recession's low point in April.

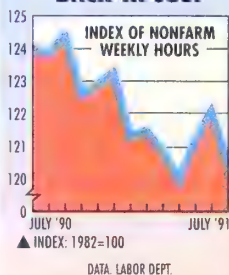
The most disturbing feature of the July employment report was a sharp drop in the workweek. Work time had risen from 34 hours a week in April to 34.3 hours in May and to 34.5 hours in June, engendering hope that the recovery was firmly in place. When companies start stretching their workweeks after a recession, it's usually a good sign that they will be adding workers in the months ahead. In July, however, the workweek tumbled back to 34.1 hours, calling further job gains into doubt.

As a result, aggregate hours worked in July fell below the second-quarter average (chart). Since overall work time is a good proxy for economic activity, that means the economy is off to a poor start in the third quarter.

Job declines last month were concentrated in services and construction. Builders handed out 22,000 pink slips, suggesting that the housing rebound may have cooled off in July. But it certainly implies that the recent strength in home construction has not offset the ongoing weakness in commercial and industrial building.

But the recovery's biggest problem could be in ser-

HOURS WORKED FELL BACK IN JULY

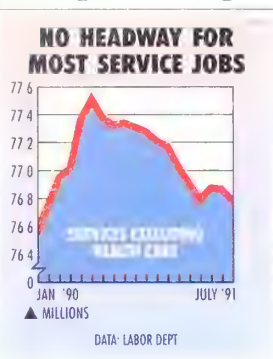


Business Outlook

vices. Service producers cut their payrolls by 41,000 workers in July. But the losses were greater than that suggests. The small, but rapidly growing, health care industry added 35,000 workers last month. Excepting that rise, service employment fell by 76,000 jobs in July, and it is no higher than it was in April (chart).

MORE JOB LOSSES MAY LIE AHEAD

Service employment could be a drag on the economy for months to come. The reason is poor growth in service productivity that is keeping upward pressure on labor costs at a time when service prices are slowing down. The result is a squeeze on profit margins that is forcing cost-cutting, and that means layoffs.



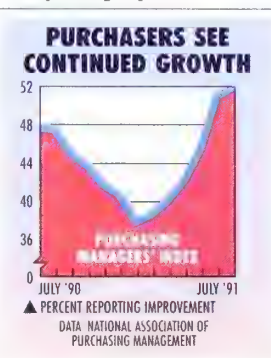
Productivity, measured as output per hour in the nonfarm economy, rose at an annual rate of 1.9% in the second quarter, fueled by a sterling gain of 3.6% in manufacturing. The overall gain was the largest in nearly three years, but that's because output per hour always improves in the early stages of a recovery, as production outpaces employment growth.

Service productivity managed to increase last quarter as well, but there has been no long-term improvement in nearly a decade. Over the year, service productivity has hardly grown. Service industries are now coming to grips with their past failures to improve efficiency, and the price of those shortcomings is service jobs.

Excluding health care, which accounts for only 10% of all service jobs, service employment is in the sharpest contraction in the postwar era. Since about 75% of all jobs are in services, an economic recovery will not be assured until service employment begins to grow again.

There is still no sign that manufacturers are ready to

start adding workers, either. Factory employment rose by 13,000 in July, but the Labor Dept. said that the count in the auto, textile, and apparel industries is because some temporary shutdowns and layoffs that usually happen at this time of year did not occur until after the government's survey period. Otherwise, factory employment would have fallen last month.



About the only upbeat report on manufacturing came from the National Association of Purchasing Management. The Purchasing Managers' Index rose to 51.8% in July, and it hovered above 50% for the second consecutive month (chart). That's a dividing line between a rising and falling factory sector.

However, other factory data aren't so reassuring. The latest survey of manufacturers' expectations by Dun & Bradstreet shows a loss of confidence in July by factories about orders, employment, and prices. A more concrete indication of that was the July drop in the factory work week, to 40.7 hours, from 40.8 hours in June. That means industrial production last month slowed from its rapid pace in recent months.

Finally, perhaps the most ominous number from the labor markets was the steep 1.3% drop in average weekly earnings in July. That means personal income apparently fell at the beginning of the third quarter. The decline comes after consumer spending in the second quarter grew three times faster than incomes. Obviously, third-quarter outlays are on a weak footing, and the recovery cannot continue if consumers don't lead it.

At best, the July job data portend an exceptionally sluggish recovery with questionable staying power. At worst, they may be saying that, for a broad swath of the economy, the recession never really ended.

THE WEEK AHEAD

RETAIL SALES

Tuesday, Aug. 13, 8:30 a.m.

Retail sales probably increased a modest 0.4% in July, according to a survey of economists done by MMS International, a unit of McGraw-Hill Inc. Higher new-car purchases in July will account for much of the gain. Sales dropped 0.2% in June but had risen by 0.8% in May.

CONSUMER PRICE INDEX

Wednesday, Aug. 14, 8:30 a.m.

Consumer prices likely edged up by just 0.2% in July, the same gain as in June. Inflation remains subdued even excluding food and energy. Such prices probably rose by 0.3% in July, following a 0.4% advance in June. Increases in the

cost of housing, in particular, have retreated sharply in recent months.

HOUSING STARTS

Wednesday, Aug. 14, 8:30 a.m.

The MMS economists expect housing starts to hold steady in July from June's lackluster annual rate of 1.04 million.

BUSINESS INVENTORIES

Wednesday, Aug. 14, 10 a.m.

Inventories held at factories, wholesalers, and retailers probably fell by 0.3% in June, after dropping by 0.5% in May.

MERCHANDISE TRADE DEFICIT

Friday, Aug. 16, 8:30 a.m.

The foreign trade deficit likely widened slightly in June, to \$4.8 billion from \$4.6

billion in May. Higher oil shipments led to an increase in imports. Exports in June probably rose, after falling in May.

INDUSTRIAL PRODUCTION

Friday, Aug. 16, 9:15 a.m.

Output at the nation's factories, mines, and utilities will post a 0.3% increase in July, says the MMS consensus. The gain could be larger because of high energy demand during the hot weather last month. In June, output jumped by 0.7% led by auto production.

CAPACITY UTILIZATION

Friday, Aug. 16, 9:15 a.m.

The expected rise in output suggests that operating rates increased slightly to 79.4% in July from 79.3% in June.

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UPHILL ALL THE WAY

CAR SALES PICK UP, BUT IT'S A GRUELING COMEBACK

When John F. Coppola strode into Jack Taylor Toyota in Alexandria, Va., in late July, he was all set. The 44-year-old government worker had studied *Consumer Reports* and had a firm idea of what he considered a reasonable price for a 1991 Celica: about \$300 over wholesale. Ninety minutes later, Coppola drove off with a nifty maroon model at more than \$1,000 below its \$14,500 sticker price. "They certainly were willing to bargain in my price range," Coppola marvels.

After the worst auto sales slump in a decade, in which Detroit's Big Three collectively lost \$7.4 billion over four quarters, car buyers are slowly returning to showrooms. As a result, U.S. car and light-truck sales have been ticking up. J.D. Power & Associates predicts unit sales for the year will hit 12.6 million, a recovery from disastrous levels during the gulf war (chart), but still way below last year's 13.9 million.

SLUGGISH MARKET. While 29% of the tire-kickers bought cars in July, up from the wartime rate of 24%, dealers say consumers remain wary. And the Federal Reserve's slight easing of credit may not help much (page 26). But if the Fed were to ease credit further, "we could have a very significant rise in auto sales," says Chrysler President Robert A. Lutz.

The upshot: No one's predicting a strong recovery in car sales. "There will be some improvement—but it will be slow," says Harold A. Poling, Ford Motor Co. chairman. Adds Richard D. Rec-

chia, executive vice-president of Mitsubishi Motor Sales of America Inc.: "The optimism we see in the market isn't supported by any enthusiastic buying. We're still pulling the customers along with incentives and rebates."

With a raft of new models coming out, General Motors Corp. may be able to hold or slightly increase its market share (table), analysts figure. But Ford and Chrysler have few new products to get buyers excited. Together, the two have lost 1.1 market-share points to Japanese rivals since January. A sluggish market will make it hard to stop the erosion. Japanese makers, with their quick, 4½-year product cycles, have a slew of all-new offerings this fall—many of them aimed at the Big Three's lucrative luxury cars and vans. Most analysts expect Japanese companies, who now have about one-quarter of the market, to gain two points a year through 1993.

Chrysler is plainly worst off. As Lutz puts it, Chrysler is "in an eternal cost squeeze." To raise up to \$500 million, it announced on Aug. 7 that it will sell 33 million shares to the public and contribute another 23 million shares to its badly underfunded employee pension plan. Chrysler is also negotiating to sell Mitsubishi its portion of their jointly owned Diamond Star car factory in Normal, Ill. Analysts figure that might raise an additional \$100 million. Also on the block are parts of Chrysler's profitable auto-finance unit and its 64% stake in a transmission joint venture with GM.



SAN FRANCISCO BUICK DEALERSHIP: TIR

Chrysler badly needs the dough to spend on new-product development. Its popular minivans are selling well, and a new version of its Jeep Cherokee is out next year. But what it really needs are new sedans, and its next generation, the LH series, isn't due until next year. "That's make or break it," says Bernard G. Campbell, director of auto analysis at DRI/McGraw-Hill. "If Chrysler can't pull it off, it has some exciting products coming out—finally."

Ford, too, has to get more new models into showrooms. Its Explorer sports utility vehicle is hot, but the popular Taurus will feature only modest restyling this fall. By the time an all-new ve-

HEADING FOR THE SHOWROOM

U. S. carmakers are racing to keep up with Japan's swift product cycles. Among the new models for 1992-93:



'92 SEVILLE: ANTISKID BRAKES AND AIRBAGS



'93 CHEROKEE: THE NEW VERSION OUT NEXT



BUT THEY MAY SUFFER STICKER SHOCK WHEN THEY GET A LOOK AT THE NEW MODELS

comes out in 1995, the car will be 10 years old. And the Tempo, which dates back to 1982, isn't due for a revamp until 1994. "Ford needs some new product," says John Hynansky, whose Winner Group is in Wilmington, Del., counts Ford among the 12 nameplates on its lot. Only GM this fall will match the Japanese car makers' proliferation of new models. There's a new Cadillac Seville, Buick Le Sabre, Oldsmobile 88, Pontiac Bonneville, and Chevy Suburban and Blazer. And GM is adding plenty of new models. For example, its revamped Pontiac Grand Am, Buick Skylark, and Oldsmobile Achieva family will have standard ABS brakes, a safety device until

now available only on much more expensive models. Air bags will be standard on many more models, too.

Some buyers may suffer sticker shock. GM has announced average 3.1% price increases, vs. Ford's 3.7% and Chrysler's 1.4%. That looks small. But in GM's case, sticker prices will rise as much as 10% on models such as the \$18,599 Pontiac Bonneville LE when air bags and other new standard equipment are included.

Meantime, Japan is applying the heat. With baby boomers becoming more family oriented, Toyota Motor Corp. will try to topple Honda Motor Co.'s Accord, the best-selling vehicle in the U.S. Toyota

has redesigned and increased the size of its Camry, while giving it a larger V-6 engine. The Camry "is perfectly positioned and executed to take advantage of what we're predicting will be a boom in family sedans," says Christopher W. Cedergren, an analyst with Santa Ana (Calif.) market researcher AutoPacific Group Inc.

Then there's the assault on the high end. Three years back, the only Japanese luxury car was Honda's Acura Legend. Two years ago, Toyota's snappy Lexus and Nissan Motor Co.'s Infiniti brands appeared. Now, there are new Japanese luxury models galore. Lexus' SC400 coupe is just out, and at \$37,700 a copy, it's a hit. And cheaper Japanese luxury models are taking on the Cadillac and Lincoln franchises in the under-\$30,000 market. Examples: Mitsubishi's just-out Diamante sedan and a more luxurious redesign of Mazda's 929 sedan that's on the way.

MORE RED INK. Trucks and vans, which Detroit now dominates, already are in the Japanese carmakers' crosshairs. Perhaps as early as 1993, Toyota is expected to deliver Japan's first fullsize pickup. And Mitsubishi is about to introduce an \$11,000 small minivan. The Japanese deny it, but Detroit has lodged charges that the Mitsubishi minivan and other models are being dumped in the U.S.

It all means more red ink. Shearson Lehman Brothers Inc. analyst Joseph Phillippi expects the Big Three to lose an additional \$1.2 billion in the third quarter and to be only "moderately profitable" in the fourth. For even if the economy's recovery gets going in earnest, the car makers' margins will remain under pressure from price slashing. To boost volume, the Japanese for the first time are offering buyers hefty discounts, too.

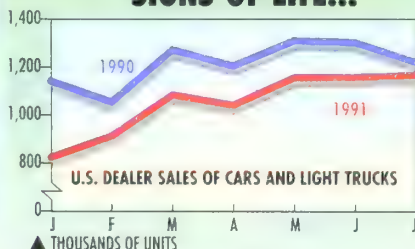
Detroit's distress, of course, means "it's a great time to buy a car," as DRI's Campbell puts it. Indeed, given the persistent pressure on carmakers, shoppers like John Coppola can count on getting sweet deals as far as the eye can see.

By David Woodruff in Traverse City, Mich., Larry Armstrong in Los Angeles, and Thane Peterson in New York



NEEDED NOW BUT DUE NEXT FALL

AUTO SALES SHOW SIGNS OF LIFE...



...BUT DETROIT IS LOSING GROUND

	MARKET SHARE*	
	MAY-JULY 1990	MAY-JULY 1991
CHRYSLER	12.1%	11.8%
FORD	23.2	22.4
GENERAL MOTORS	36.7	36.6
TOTAL BIG THREE	72.0	70.7
TOTAL ASIANS	24.6	26.6
TOTAL EUROPEANS	3.4	2.7

*CARS AND LIGHT TRUCKS, INCLUDING CAPTIVE IMPORTS



IT'S NOT MUCH OF A CUT, BUT IT'S A CUT

The Fed funds rate may need to fall more, though, to avert a double dip

In mid-July, a senior Federal Reserve official relaxed on the couch in his office and listed the reasons the central bank could take it easy for the summer. The economy was recovering but not fast enough to revive inflation fears. Financial markets were quiet, and so was the bickering among Fed factions. "We have a pretty good period ahead of us," he said. But, he added, "you can't predict this recovery very well."

No kidding. Three weeks later, the Fed was buffeted by a sharp drop in the money supply, declining employment, and renewed pressure from the Bush Administration for easier money. On Aug. 6, the Fed responded with a cut in a key determinant of interest rates—the cost of federal funds, or overnight loans between banks. While the drop from 5.75% to 5.5% was small, it was the Fed's first easing since Apr. 30. "The economy is very weak, and it desperately needed this," says Robert A. Brusca, chief economist at Nikko Securities Co. International.

RALLIES. Wall Street welcomed the move as a signal that the Fed was trying to head off a second dip into recession. The Dow Jones industrial average finished the day up 38.24 points. Bonds also rallied, despite a heavy

supply of new issues. "The stock market liked it, the bond market liked it, business liked it, President Bush liked it," said Joseph A. Wahed, chief economist at Wells Fargo Bank. "I only hope the Fed liked it enough to do it again."

Inside the Fed, however, officials weren't pitching their move as the start of another round of recession-fighting. "This was a technical move to execute existing policy," a top official insists. The central bank hasn't quit trying to squeeze out inflation. Nor is it wavering in its belief that a modest recovery is on the way. Its regional economic survey, released on Aug. 7, concludes that "national economic conditions continue to improve, but at a slow, uneven pace."

Against that backdrop, a slide in the money supply had Fed officials asking if they were doing enough to support the

recovery. M2, which measures currency and checking, savings, and time deposits, dropped at a 2.8% annual rate from June to July (page 21). As a result, it had grown at a 2.7% rate since December, close to the 2.5% bottom of the Fed's target range. Meanwhile, the Labor Dept. reported a loss of 51,000 jobs in July, accompanied by slow growth in labor costs (charts). "Money alone wasn't enough of a reason to ease," says a Federal Reserve Bank president who is a hawk on inflation. "But with the employment numbers and soft inflation, it seemed like we could buy some recovery insurance at a modest cost."

DOLDRUMS. After Friday's jobs report, Fed Chairman Alan Greenspan spent the weekend calling other Fed officials. At the central bank's camps—monetarist watchers of economic statistics, and inflation superhawks—saw the need to move. Greenspan decided to act swiftly rather than wait until the Aug. 20 meeting of the policy-setting Federal Open Market Committee, because a rate cut now would have more impact than one in late August's market doldrums.

On Aug. 20, the key issue will be: Has the central bank done enough? The latest move probably won't spur the torpid economy into a new spurt of activity. Home buyers and blue-chip corporate borrowers will feel the effects immediately: The rate on 10-year Treasury notes, a key indicator of mortgage rates, fell to 7.94% at the Aug. 7 auction, down from 8.01% two days earlier. But other borrowers won't be so lucky. Bankers are likely to use the Fed's move to boost profits, not cut loan rates.

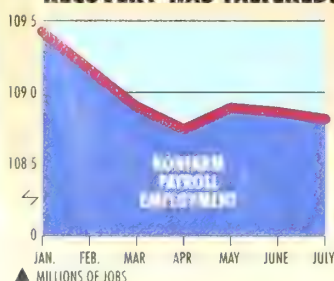
To stimulate business—and to prevent the double-dip recession the GOP fears—the Fed may have to cut again in September. That step will be harder because the central bank also would have to cut its highly visible discount rate, now at 5.5%, to keep it below the Fed funds rate. Another cut would also raise fears the Fed is staying easy too long.

History shows that past Feds have overheated the economy by doing just that. But history also shows that "the Fed has overdone its easing policy a bit," says Robert J. Bera, chief economist at Lehman Brothers Inc. "The economy needs enough thrust to escape gravity, before it can cruise." The Greenspan Fed might be better off with one easing step than many more than one too few.

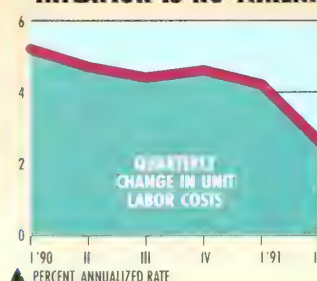
By Mike McNamee in Washington, with William Glasgall in New York

WHAT GAVE THE FED WIGGLE ROOM

THE JOB MARKET'S RECOVERY HAS FALTERED...



...AND WAGE-BASED INFLATION IS NO THREAT



DATA: BUREAU OF LABOR STATISTICS

SECURITY PACIFIC'S SAFETY NET IS FRAYING FAST

Real estate loans are straining its already slim loss reserves

When Robert H. Smith became chief executive of Security Pacific Corp. last year, his big challenge seemed to be finding a way to improve on his predecessor's stellar record. Under Richard J. Flamson the Los Angeles-based banking company had quadrupled its assets, to \$84 billion, and aggressively expanded into retail merchant banking. Soon after taking charge, Smith returned from a management brainstorming session in Palm Springs with promises to boost the stock and push Security Pacific into a fresh era of bank acquisitions. Promises, promises. For Flamson's legacy to Smith seems to be a slew of problems. To the tune of a \$200 million write-off, Smith late last year announced he would slash Security Pacific's international lending and securities-trading operations. Meanwhile, loans on highly leveraged deals were going bad, including a big one to troubled Hawaiian Airlines Inc. A glut of real estate loans pulled from Britain and Arizona. Profits fell last year, to \$161 million—and another in the first half of 1991.

INNOUS: The latest rumormongering is coming in Security Pacific's own backyard. Bad loans in California real estate are beginning to take a toll. Security Pacific said in July that about half of the \$3 billion in loans it classified as nonperformers in the second quarter are California real estate loans. That hurt the stock. But the bad news just keeps coming: On Aug. 2, Keefe, Bruyette & Woods Inc., a prestigious bank research firm, forecast further real estate loan losses in California. When the stock went down again, this time by about 5% in a day.

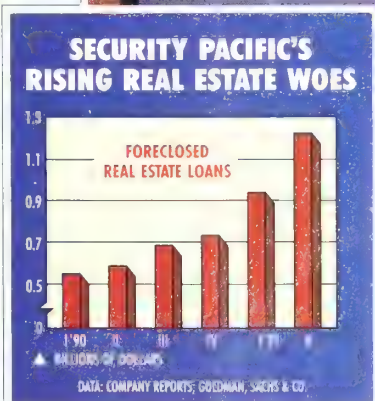
All California banks are struggling in the Golden State's recession, but Security Pacific has stood out for its reluctance to concede any worries. They are not as far along in recognizing

their problems as other California banks are," says Sandra Flannigan, an analyst at Alex. Brown & Sons Inc. She points to its low level of loan-loss reserves relative to its troubled loans: 58% at Security Pacific, compared with an average of 82% nationally. Crosstown rival First Interstate Bancorp has bent over backward, with reserves amounting to 115% of its nonperforming loans.

Smith and other Security Pacific executives declined to be interviewed. But in



CEO SMITH: THE "FAT AND FANCY" DAYS ARE OVER



the past they've said the bank keeps lower reserves because it has already aggressively written off some bad loans and that it has solid collateral to back others.

Just the same, Security Pacific's reserve ratios are thinning as its loan portfolio is turning sour. Nonperforming loans and foreclosed real estate jumped to 6% of total loans and foreclosures at midyear, compared with 4% nine months earlier (chart). Growth in nonperformers even outpaced the bank's hefty charge-offs of bad loans—\$933 million during that period—notes David C. Cates, president of Cates Consulting Analysts Inc. "That's a fairly ominous sign," he adds. Donald K. Crowley, the Keefe Bruyette analyst whose report shook investors, expects

bad loans to grow by another \$600 million to \$700 million in the second half.

Security Pacific earlier this year was forecasting a second-half turnaround in California's economy. Analysts now think it could take longer. "It may be mid-1992 before it turns," says Claire M. Percarpio, a credit analyst at Duff & Phelps/MCM Research Co. California suffered later than most of the nation, and it will likely rebound later, too. Moreover, Flannigan notes, loan troubles tend to lag behind turns in the economy: "The problems have not yet peaked."

Looming loan problems may have squelched Security Pacific's merger talks with Wells Fargo Bank. When negotiations broke off last December, many analysts suspected that the hard-nosed San Francisco rival had been spooked by the unknown depths of Security Pacific's loan problems. Neither side

would comment on why the talks ended.

WINDOW SHOPPING. Despite its continued optimism about an impending upturn, the bank's shares, now around 23, are 58% below their August, 1989, high of 54%. And when it comes to mergers, a bank's stock is its "currency," as Smith likes to call it. Security Pacific's weak currency means its managers must stand by while such rivals as Bank of America, which went through its own crisis in the mid-1980s, use their stock to scoop up banking units at bargain prices. On July 31, BofA announced plans to buy Valley Capital Corp., parent of Nevada's No. 2 bank, in a deal valued at \$400 million.

Smith gets high marks from industry analysts for his

handling of the problems he inherited from Flamson. His task involves a basic repudiation of the fast-growth, global expansion policies that had guided the bank during the previous decade. Smith also has Security Pacific backing away from its strategy of limiting interest-rate risk in favor of fee-based businesses, such as the merchant bank.

The bank's future, Smith said at the April annual meeting, is in its traditional role as a big retail and commercial lender in the West. "We envision ourselves getting back to our core businesses," he said, "not fat or fancy." Keefe Bruyette's Crowley is impressed: "I have to give him credit for being willing to turn the company upside-down," he says. "He's doing what needs to be done, and it's a dirty job." And it's hardly the job he expected when he returned from his desert sojourn to Palm Springs.

By Kathleen Kerwin in Los Angeles

WILL BOEING BUILD A BEHEMOTH TO DEFEND ITS TURF?

To ward off Airbus, it's considering a superjumbo successor to the 747

Ever since rival Airbus Industrie stirred up the Paris Air Show in June with talk of building an airplane larger than Boeing Co.'s huge 747-400, Boeing officials have shied away from the subject. Yes, such a plane would challenge the monopoly franchise enjoyed by Boeing's humpbacked giant. And yes, Boeing was studying its own alternatives. But that's about all the nation's No. 1 exporter would report.

Now, however, Boeing is sending signals that a new "superjumbo" jet is a real possibility. It has formed a special unit to study the question and has assigned its top marketing executive, John B. Hayhurst, to head up the effort. Meantime, Boeing is talking to Japan's three leading heavy manufacturers about chipping in on development of a superjumbo and other planes. At a time when the airline industry is suffering an unprecedented financial crisis, spending billions on a new project seems risky at best. But, says the 43-year-old Hayhurst, "If we believe this is a substantial market, we'll find a way to develop it."

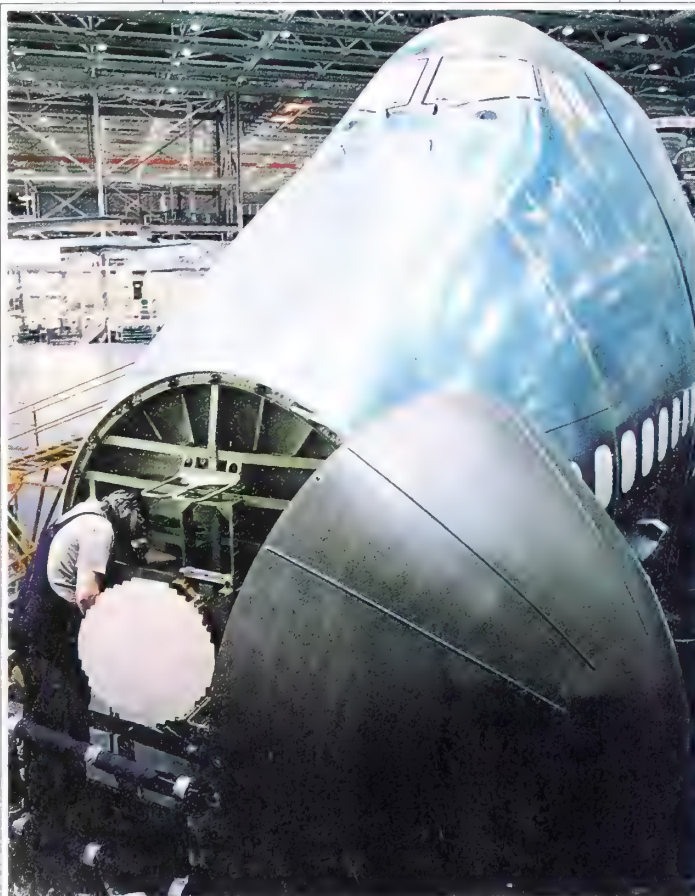
LONG SHADOW. Boeing may have to. Airbus clearly put Boeing on the defensive in June when Managing Director Jean Pierson said the European consortium was accelerating study of a plane bigger than the 747, seating 600 to 700 passengers. Although it couldn't launch such an ambitious project until 1994 at the earliest, Pierson was aiming at Boeing's jugular. Boeing's big-plane monopoly allows it to reap margins as high as 40% to 50% on the 747-400, which lists for up to \$152 million. That big edge helps Boeing compete aggressively at the lower end against Airbus, which is government-owned and funded. "It would be the first time we would be able

to go after their cash cow," says John J. Leahy, Airbus' U.S. sales chief.

The superjumbo market could be lucrative, indeed. Stephen M. Wolf, chairman of United Airlines Inc., surprised Boeing in early June by publicly asking it to consider making a 650-seater for delivery by 1997 or 1998. And although American Airlines Inc. is skeptical, Boeing says many major Asian airlines

casting a long shadow over Boeing's \$92.6 billion backlog. And just last October, Boeing formally launched another big project, the 777, a widebody model somewhat smaller than the 747. The 777 is gobbling up most of Boeing's \$1.5 billion in research-and-development costs this year, as well as engineering, marketing time and effort. All told, it will cost Boeing at least \$4 billion, siphoning profits for the next few years.

STRETCHED. That's where Japan comes in. Already, Japanese manufacturers are funding 20% of the 777's total development and will build big portions of the jet's fuselage. A similar agreement on the superjumbo could help defray a development burden that might amount to \$5 billion—some analysts say more. The Japanese might ease a



ON BOEING'S LINE: LAUNCHING A SUPERJUMBO COULD COST \$5 BILLION



HAYHURST: STUDYING THE OPTION

BOEING'S SUPERJUMBO CHALLENGE

SIZE 600-800 seats, possibly on two decks

MARKETS High-density overseas routes such as New York-Tokyo or New York-London, with focus on the Pacific

COST At least \$4 billion to \$5 billion, assuming a plane developed from scratch

RATIONALE To move more people between airports with increasingly limited takeoff and landing space

DATA: BW

have expressed desire for the plane as well. The most obvious need for a superjumbo is on heavily traveled long-distance routes, such as those across the Pacific and the North Atlantic. Congested airports in Tokyo, London, and New York cannot handle many more planes, but they could handle more passengers on bigger planes.

Still, it's an awkward time for Boeing to consider a new aircraft. The grave financial health of the airline industry is

strain, but building a superjumbo would tax Boeing's resources all the same.

Boeing has turned up the heat in Washington in response to Airbus' market-share gains and talk of building a superjumbo. The Seattle company is lobbying to have the consortium's European subsidies declared illegal under the General Agreement on Tariffs & Trade. But the European Community is stonewalling and may yet decide to ignore any unfavorable rulings. Moreover

Boeing also is loath to irritate its European-airline customers—or Airbus suppliers in the U.S.—its defense is a competitive product.

Dayhust's job will be to recommend whether it would be best to modify the 747 or go with an all-new design. The 747 could be stretched by adding a hump-shaped section of fuselage to the middle of the plane, making it long enough to install 85 more seats. Or Boeing could extend the 747's hump into full-length upper deck, making it look like a winged double-decker bus. Those options would save money, and either could produce a plane as early as 1997. But neither alteration would add more than about 15% to 20% to the 747's capacity, and both would shorten the 747's range and fuel efficiency.

TTOP. An all-new plane—possibly based on the 787—would mean designing a new wing to solve the range and efficiency problems. Flatter on the top and wider on the bottom, a new wing would probably be longer, thicker, and swept-back than the current 747 wing. The plane would likely use lightweight composite materials and higher-powered engines. Boeing would also equip it with advanced avionics, including electronic "fly-by-wire" controls, which eliminate mechanical cables and pulleys. On the 777, the superjumbo would be able to have a flexible, high-tech interior with amenities such as seat-back entertainment screens and telephones at every

seat, says Airbus. Airbus would not launch a superjumbo unless it was significantly more efficient than the 747. The goal: more seats without a corresponding increase in the amount of fuel burned. The solution the Europeans are considering involves squishing two Airbus airbodies together side-by-side. The resulting oval-shaped fuselage—curved on the side but relatively flat on the bottom—would act as part of the wing itself, increasing lift. The concept, similar to that used on the space shuttle, would allow a wider body with the same length wing. Such a plane could have as many as 18 seats abreast, divided by narrow aisles, and still be able to squeeze through airport gates designed for the 747. Given the huge financial commitment, both Airbus and Boeing are likely to study the superjumbo very carefully before jumping. What's certain, however, is that one day the 747 will become obsolete, and both manufacturers want to have a product ready to replace it. "This is a business segment Boeing is not going to cede to anybody," says analyst Lawrence M. Harris of Kemper Security Group. Perhaps. But the cost of do-or-buy battle with Airbus may be as stunning as the size of the superjumbo itself.

By Dori Jones Yang in Seattle

THROWING STONES AT THE 'GLASS CEILING'

The Labor Dept. is about to start investigating federal contractors

The Labor Dept. has made official what many employees have known for a long time: A "glass ceiling" of often subtle attitudes and prejudices has blocked women and minorities from climbing the corporate ladder. On Aug. 7, Secretary Lynn Martin unveiled plans to begin investigations of federal contractors to ensure companies are doing all they can to remove race- and gender-based obstacles to upper-echelon jobs.

The move follows an 18-month study of promotion practices at nine large corporations. The probe found that the height of the glass ceilings varies from company to company, some not far above entry-level positions. Minorities hit plateaus at lower levels than women. Martin says problems were most severe at companies where the chief executive had not taken an active role in advocating strong affirmative-action policies. "It's quite clear that if the person at the top is not interested, it won't work," Martin says.

The Labor Dept. conducted the study so that it could understand how managers make promotion decisions. Now, its Office of Federal Contract Compliance Programs will begin full-fledged enforcement. The office already conducts affirmative-action reviews of entry-level hiring by 250,000 contractors that do \$200 billion worth of business with Uncle Sam. Last year, it scrutinized 6,033 companies. Martin said Labor will do far fewer glass-ceiling investigations because they're far more complex and time-consuming. But they'll be backed by the same penalties, including disqualification of companies that refuse to correct discriminatory practices.

FLEXIBLE. Employer groups had worried that Labor wouldn't understand differences in corporate cultures and that it would issue standardized remedies for everyone. But Labor officials vow that the solutions they'll suggest will fit a company's traditions. For instance, one unidentified company that was studied requires all senior executives to have 25

years' experience. Rather than demand that the company promote someone with less experience, Labor tried to ensure women and minorities were being groomed for those roles down the road.

Such flexibility will come as a great relief to corporate management. "If they had come with a template, it would not have been well-received," says Susan R. Meisinger, a Society for Human Resource Management lobbyist. "It sounds like they will be helping companies figure out what to do."

The Labor report identified several barriers that help explain why women account for only 6.6% of corporate executives and minorities hold a paltry 2.6% of executive jobs. In some cases, companies used headhunters who failed to pursue qualified candidates who weren't white men. Recruitment practices often relied on word-of-mouth and employee referral. Such networking by white men usually excluded female and minority candidates.

GOOD TIMING. In many cases, the study found, women and minorities were not given the crucial early training that could make promotion possible. Also, women and minorities were frequently passed over for the high-visibility special projects that could let them make their mark. And in companies where mentoring played an especially prominent part in giving employees a leg up, white males often sought to help people like themselves.

The Bush Administration has released its glass-ceiling report at the same time it is battling Democrats over other politically charged race- and sex-discrimination policies. President Bush has threatened to veto a civil rights bill that would make it easier to pursue discrimination cases in court. And he is pressing his nomination of Judge Clarence Thomas, a foe of affirmative-action programs, to the U.S. Supreme Court. The timing may be coincidental, but the glass-ceiling initiative won't hurt a bit as critics of his civil rights record bear down on Bush.

By Susan B. Garland in Washington



MARTIN: REMEDIES THAT WILL FIT THE CORPORATE CULTURE

A DIRECT HIT IN THE WAR ON CANCER

Researchers uncover the gene that triggers colon polyps

Colon cancer is a terrible scourge. It strikes more than 155,000 Americans each year. And with an annual death toll in the U.S. of 60,000, it's second only to lung tumors as a killer of cancer victims. That's why scientists have been probing genes in an effort to find the fatal strands of DNA that lead to colon tumors. Over the past few years, they've identified three of the genes that, when altered, are cancer time bombs. Now, two research teams may have nabbed the trigger gene, the one that touches off the cascade of changes on the cellular road to cancer.

Once scientists figure out how the newly identified gene brings on the deadly process, they may be able to design drugs that can block the chain of events. That could dramatically reduce the death rate from the disease, which now is treated with the standard "cut, burn, and poison" approach of surgery, radiation, and chemotherapy.

The discovery, announced on Aug. 9 in a series of scientific papers in the journals *Science* and *Cell*, also comes with a darker side. Scientists think that the flawed gene is inherited by one in 5,000 people. And they are devising ways to search for it even before birth. "It brings up a whole set of troubling ethical questions," says Johns Hopkins University oncologist Bert Vogelstein, leader of one of the teams.

ALTERED STATES. Identifying the gene, named APC for adenomatous polyposis coli, highlights the remarkable progress science has made in understanding the genesis of cancer. It turns out that colon cancer is an ideal candidate for scrutiny because it occurs in several distinct stages. The first is the growth of tiny lumps or polyps in the lining of the colon or rectum. Former President Ronald Reagan made this condition famous in 1985, but doctors estimate that 40% of us will have one or more polyps at some point in our lives. Fortunately, only 10% of those with polyps will progress to the next stage of the disease, when the pol-

yps turn into malignant tumors. The final stage occurs when the tumor cells spread beyond the colon to other parts of the body.

Researchers, including Vogelstein and Raymond White at the University of Utah, have been able to show that different genes act at different stages of the disease. Most of the genes previously identified seem to play a role in the final stages. When altered, they cause a benign polyp to turn into a malignant

ety of environmental factors—from exposure to specific chemicals or radiation to the accumulated defects of the aging process. The result is a biochemical change that leads to polyps.

The crucial question that remains is why alterations in the gene set off a series of steps leading to cancer. To answer that, scientists must find out what the correct version of the gene normally does. "The function of the gene is almost a totally open question," says Vogelstein.

TESTING AND ETHICS. Turning the discovery into new therapies also will await a better understanding of how the gene works. But, White notes, for families affected by FAP, doctors will soon be able to tell who has inherited the gene. "The notion of testing the unborn for a gene—or other genes that predispose people to cancer—raises such trouble-



VOGELSTEIN LED THE RESEARCH TEAM AT JOHNS HOPKINS

THE CULPRITS IN COLON CANCER

Researchers believe that anywhere from 6 to 10 different genes may be involved in the progression of colon cancer. The following four have been identified so far

Gene	Role in disease
APC	Formation of polyps
RAS	Transformation of polyp to tumor
DCC	Late-stage malignant tumor
P53	Malignant tumor and spread of cancer

DATA: BW



WHITE LED THE RESEARCH TEAM AT THE UNIVERSITY OF UTAH

tumor and spread throughout the body (table).

APC seems to control the crucial first step to colon cancer. The evidence is twofold. First, after years of genetic sleuthing, White was able to show that the gene was linked to an inherited disease called familial adenomatous polyposis, or FAP. By the age of 30, victims typically grow a veritable carpet of polyps in their colons and must have the organ removed. By testing the DNA in large families with the disease, White discovered that many of the victims had inherited flawed copies of the APC gene.

The second key piece of evidence comes from Vogelstein's group. The Johns Hopkins researchers found flawed versions of the APC gene in polyps and tumors sliced from people who get the more common, nonfamilial form of the disease. What apparently happens is that the gene can mutate, due to a vari-

ety of environmental factors, questions as whether parents will want to give birth to children who have a good chance of developing cancer at an early age. In addition, there's worry that people with these genes won't be able to afford health insurance. But for people at risk for noninherited colon cancer, usually because they eat lots of fat, a diagnostic test could be a lifesaver. "Early diagnosis is very important, because only by removing polyps can you reduce the chance of cancer," says White.

For many researchers, colon cancer is just a first step. They believe that some of the same or similar genes are the culprits in other stubborn cancers such as those of the breast and lung. And as they begin to unlock this deadly mystery, they are getting closer to stopping cancer where it starts.

By Naomi Freundlich in New York and John Carey in Washington

It was an unlikely alliance.

But when five state governments, two wildlife conservation groups and one energy company came together, 32 species of threatened wildfowl secured a brighter future.



The partnership called itself The Playa Lakes Joint Venture. Its mission, to enhance and protect the wetlands resource of the Playa Lakes region critical to wildlife.

Boosted by grants from private landowners, state wildlife agencies in Texas, Oklahoma, Kansas, New Mexico and Colorado, with the U.S. Fish & Wildlife Service and Ducks Unlimited, Inc., matched donations from Phillips Petroleum to protect vital avian breeding and migrating habitats. Habitats that with resources and restoration could slow the dramatic decline of millions of ducks, geese and cranes from lack of water.

It was an unlikely alliance. But when five state governments, two wildlife conservation groups and one energy company came in with concern and came out with solutions, it seemed more inspired than unlikely, after all.

PHILLIPS PETROLEUM COMPANY 

For more information about what we are doing to protect our environment, write: Playa Lakes, Phillips Petroleum Company, 16C4 Phillips Building, Bartlesville, Oklahoma 74004.

Commentary/by Peter Coy and Michele Galen

LET'S NOT LET PHONE POLLUTION HANG UP FREE SPEECH

The government is having a heck of a time deciding how to approach dial-a-porn. Is it corrupting America's children? Protected by the First Amendment? Or both? Congress has made three stabs at the issue. The latest set of federal laws and rules on dial-a-porn was upheld this year by appellate courts in New York and San Francisco. But few people think the matter has been laid to rest.

So emotional an issue always tends to muddy the legal waters. But another reason for the muddle over dial-a-porn is the growing number of roles taken on by the telephone. Today's network, no longer just a conduit for conversation, is carrying things Alexander Graham Bell never imagined: news, electronic mail, and computerized sales pitches, to name a few. But the courts haven't kept up with technologies that have implications for free speech and privacy rights.

TROJAN HORSES? The variety of uses for the telephone system inspires awe. Recorded soap-opera updates or dial-a-porn are more like radio broadcasts than a telephone conversation in that everyone who calls hears the same thing. Tellingly, these recorded messages are called shows. The phone network can also serve as a postal system via electronic mail. Electronic bulletin boards present their own cluster of legal issues. And the surge in telemarketing—transformed by random dialers and robot salespeople—raises questions about whether marketers have managed to turn home phones into Trojan horses for sales pitches.

As society goes electronic, contacts that used to occur in the town square are being made over phone lines. The problem is that there's no simple standard for deciding what can be said or even who should decide. Often, phone companies end up calling the shots by agreeing or not agreeing to bill and collect for services offered by outsiders over their networks.

With 900 numbers, which range from stock market quotes to sports scores to soft porn, each long-distance

carrier sets its own rules. U.S. Sprint Communications Co. recently decided to let "romance" and "dating" 900 lines fade away through attrition by not billing or collecting for any new ones. The lines are used by all kinds of people, not just Sprint's regular customers. Sprint has been braver about billing for outsiders' political messages, which



have ranged from pro-David Duke to anti-Jesse Helms. Still, Sprint calls the shots. If all four long-distance carriers that offer 900 lines turned squeamish about a service, they could effectively shut off an outlet for free speech.

The kind of picking and choosing that long-distance companies engage in is an even bigger headache at the local level, where information providers don't have a choice of carriers. And even though many states require local phone companies to make their billing and collection services available to all, the carriers can still find ways to make

life tough for information providers they find unsavory, such as pressing for laws restricting them.

There is a solution. Since the main problem is that phone companies don't want to bill and collect for services that could tarnish their reputations, companies that provide these services should do their own billing and collecting.

It's more expensive, but there's nothing in the Constitution that promises dial-a-porn vendors, gab-line operators, or vendors of "guaranteed" credit cards that someone will inexpensively collect their money for them.

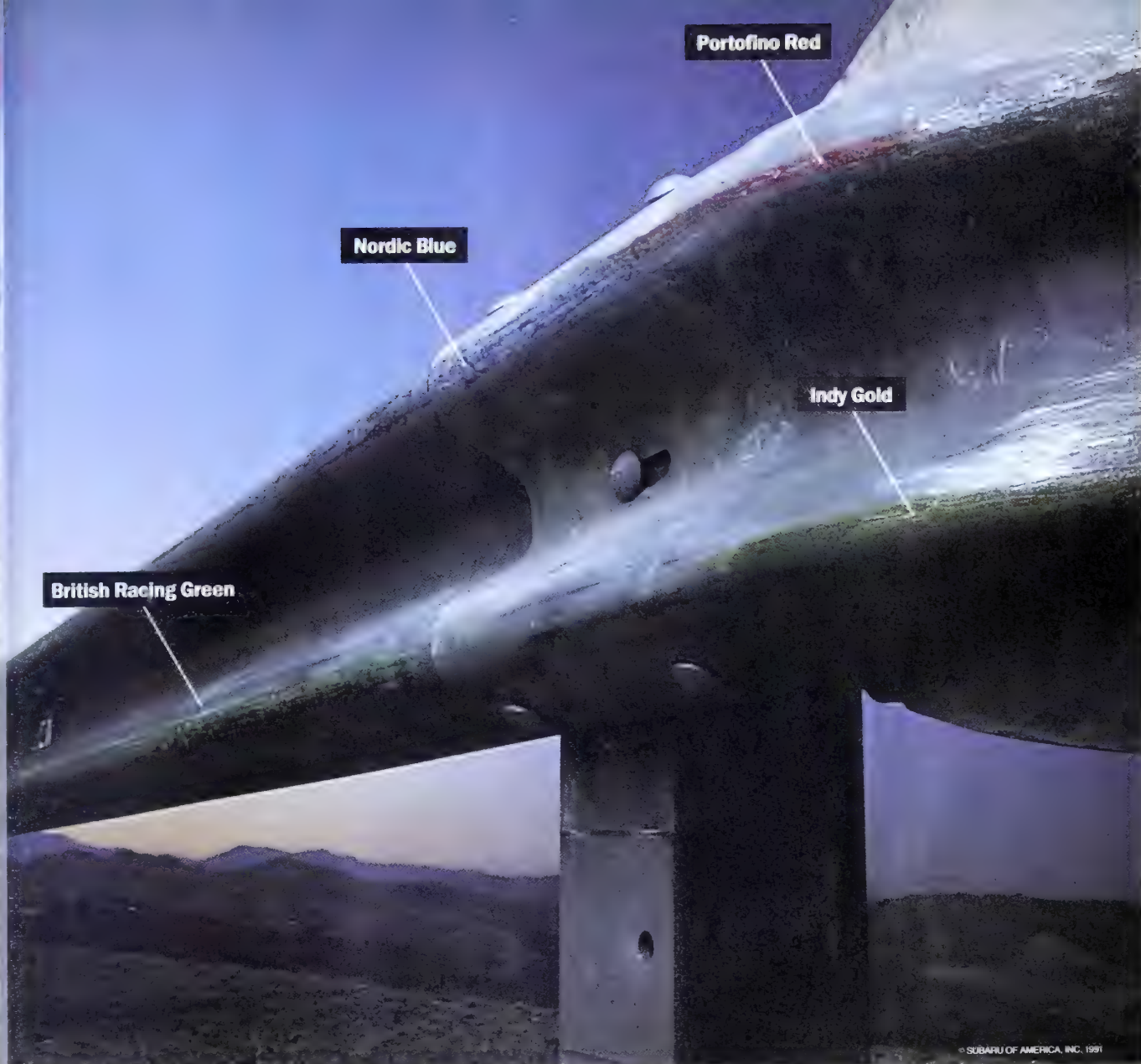
FAIR CHANCE. Other conflicts turn out to be similarly solvable. For example, it's possible to protect children from pornography or ripoffs and still preserve adults' First Amendment freedoms: Just have phone companies hand out passwords to customers 18 and over, no application required. The easy-to-use pushbutton codes would be required to reach "adult" services or lines supplying highly priced information. It's not foolproof, but then, underage kids also find ways to buy liquor and sneak into X-rated flicks.

Keep in mind, too, that these measures wouldn't open the wires to truly obscene or fraudulent services: Those are and would remain illegal. But with independent billing and passwords, services that are merely risqué or mildly suspect would get their fair chance in the marketplace of ideas.

Electronic communications should not be treated any differently just because they arrive over phone lines instead of in the mailbox. Laws protecting U.S. mail can—and should—protect messages delivered over public electronic mail networks. In contrast, a telemarketer's computer-generated call at dinnertime doesn't deserve the same legal protection as a phone call from Aunt Martha, even though it happens to use the same medium.

As phone networks are put to ingenious new uses, they may seem ungovernable. But the rules that can control them and everything offered over the wires are already here. They're just waiting to be applied.

Phone lines are no longer
just phone lines.
They are the town square
of the Electronic Age



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WHAT THIS TOWN NEEDS IS . . . NUCLEAR WASTE?

Martinsville, Ill., ponders the pros and cons of a radiation dump

Max Cruse sips coffee and stares out across the soybean fields bordering the Hen House Restaurant in tiny Martinsville, Ill. "This town will die without that thing," he says. Down the road, the folks in Kona Morrill's farmhouse think differently. "It could kill us," she insists. Chimes in teacher Steve Cloud: "The town's gonna die, anyway."

Martinsville, a depressed 1,100-person hamlet 170 miles south of Chicago, is on the verge of communal meltdown. The issue? Whether the town should become home to Illinois' low-level nuclear radiation dump. In one corner: townsfolk who believe the economic lift provided by the 1,400-acre waste dump could save Martinsville. Their sworn opponents: locals who fear the effects of radiation.

SLAIN CATTLE. It's not a friendly fight. People say the battle has produced slain cattle, shot-up mailboxes, and death threats. It has even split families. "My brother supports the dump," says Morrill. "We haven't spoken in over a year."

The town's predicament isn't singular. Across the farm belt, hundreds of small towns have tried to stave off dissolution by latching on to public-works projects such as prisons and landfills. Now, states are providing another lifeline: dumps to hold low-level nuclear waste from such things as reactors and hospitals. Compelled to find local homes for nuclear waste by 1993, states including Illinois, New York, and California are offering cold, hard cash and the promise of jobs to desperate towns.

Martinsville city officials have begged for the dump since Illinois started searching for a site in 1987. Small wonder: The once-bustling Clark County town has seen its fortunes slide since the mid-1970s, when Interstate 70 bypassed it. Unemployment has hovered at

14% for years. Two years ago, the town lost its bank; this year, the newspaper folded. Townsfolk fret that the high school, with an enrollment of 115—50% less than a decade ago—will go next. "If it goes, we're gone," says resident Joe Boyer, who wants the dump.

Many townspeople welcomed the Illinois Nuclear Safety Dept. when it blew into town three years ago. The agency promised that whichever town hosted the dump would rake in user fees of at least \$1 million a year from its manager,

Farmers John and Kona Morrill: 'My brother supports the dump,' she says. 'We haven't spoken in over a year'



Chem-Nuclear Systems Inc., a unit of Waste Management Inc. That's big money for a town with an annual budget of \$540,000. In addition, said the Nuclear Safety Dept., the dump would create 100 jobs, most paying over \$20,000 a year.

The town is already getting a taste of the money the dump would bring in. The state, using a kitty funded by fees levied on Illinois power companies, has pumped \$1.2 million into Martinsville since 1988 to pay for the disruption caused by planning for the dump. "They're trying to buy us," charges Morrill. "Nonsense," scoffs Mayor Truman Dean. "We're just gettin' paid for our troubles."

Dean is certainly making the most of it. The city has given \$200,000 to the

school district, which bought computers and fixed the high school roof, and spent \$24,000 for new police cars. The American Legion got \$3,000 for a new freezer. And each citizen of Martinsville got \$50 last winter to apply toward December utility bills. Meanwhile, the state gave rich contracts to locals, including \$160,000 over two years to Dale Huffington, who runs a Clark County economic development firm.

BAKE SALES. The cash hasn't softened the opposition. Concerned Citizens of Clark County raised \$8,500, mainly through bake sales, to fund a study of the farmland selected by the state to house the dump. The study concluded that radioactive waste from the proposed site, roughly a mile from Martinsville's main street, could leak into the town's groundwater. Proponents reason that the facility's state-of-the-art engineering will eliminate any risk of leak-

A state commission is supposed to solve the dispute after hearings in mid-August. A decision is expected before yearend.

Meanwhile, back at Morrill's kitchen table, dump opponents are talking about a speech Huffington prepared in 1988, a draft sent to the Nuclear Safety Dept. Huffington wrote that a containment pond for potentially radioactive water "will be a good source of recreation." Although Huffington deleted the remark, Morrill is scornful. "Those people don't know what they're talking about," she says. With or without the dump, the wounds from this battle could bleed Martinsville to death.

By Kevin Kelly in Martinsville, Ill.

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EDITED BY HARRIS COLLINGWOOD

WHO'LL GET PAN AM? IT'S STILL UP IN THE AIR

► Nobody ever said Pan Am would die quietly. After two weeks of offers and counter-offers from various quarters for the bankrupt airline's assets, Pan Am Chairman Thomas Plaskett chose a \$310 million bid from Delta plus a cash infusion to keep the carrier running. He then asked the Transportation Dept. for a speedy transfer of Pan Am's European routes and North-east shuttle.

But it's almost certain Plaskett's plan won't fly. Rumors are rampant of potential new deals featuring many a strange bedfellow. Sources in Washington say United, arch-rival American, and TWA will jointly bid to buy and split up all of Pan Am. Another rumor has Delta, Continental, and Northwest readying a competing bid. Never mind that Continental is in Chapter 11 and Northwest is deeply in debt.

It's hard to imagine United and American teaming up, but United's Stephen Wolf, American's Robert Crandall, and TWA's Carl Icahn were seen huddling during an Air Force bash celebrating the airline industry's contribution to Operation Desert Storm. "Anything is possible," says a senior airline executive, who admits the three carriers might be talking. "This will go up to the last minute." Bids are due on Aug. 12.

BRANIFF GOES UNDER—AGAIN

► Speaking of airline bankruptcies, guess who's back? Braniff, of course.

After going bankrupt twice in the 1980s, the once-proud Dallas carrier was liquidated. Real estate investors Jeffrey Chodorow and Arthur Cohen—who led Braniff into its second filing—then bought the name and attached it to a charter carrier they had purchased. They launched the

new Braniff International Airlines on July 1, with dreams of serving New York and Los Angeles out of Dallas. The dream lasted until Aug. 7, when Braniff filed for Chapter 11 again. Only in the airline industry.

TIME WARNER'S OFFERING FLIES

► Time Warner can finally start whittling down its \$11.2 billion debt. On Aug. 6, it completed a modified offering to raise \$2.76 billion. The company's investment banks snapped up rights to buy 42% of the shares sold. As a result, 98% of Time Warner's shareholders participated, either by buying shares or by selling their buying rights to the syndicate of banks led by Salomon Brothers.

Time Warner sold about 34.5 million new shares at \$80 each. The offering replaced an earlier proposal that Time Warner scrapped after protests by angry shareholders and the Securities & Exchange Commission.

A BUYER FOR EXECUTIVE LIFE

► On Aug. 6, four months after seizing Executive Life Insurance of California, state Insurance Commissioner John Garamendi signed an agreement to sell Executive Life's policies and other assets to a

SEE DAN. SEE DAN LOOK FOR WALDO

Check out the front page of the paper: The politicians are preparing for next year's Presidential election. Scan the best-seller list: "Waldo" books as far as the eye can see. Put the two phenomena together, and you get *Where's Dan Quayle?*, a take-off on the *Waldo* series.

Like the *Waldo* books, *Where's Dan Quayle?*, by Jim Becker and Andy Mayer, is really a game. The object: Find the Veep among the goofy characters populating an illustration. The rendering of the 1988 G convention features delegates from Pluto, a vendor selling coffee on a stick, and a note from Quayle asking: "Does t mean I get an honorary degree from the Electoral College?"

Collier Books Editor-in-Chief Mark Chimsy expects 1 things from this book, due out on Sept. 12. "People are starting to think about the election," he says. "And when we think about the Vice-President, we all get a little nervous, don't we?"



French group led by Paris-based insurer MAAF. At the same time, Garamendi sold Executive Life's junk bonds to Altus Finance, an investment arm of Crédit Lyonnais, for \$2.7 billion. At a press conference announcing the transactions, Garamendi also confirmed that the U.S. Justice Dept. is investigating Executive Life's pre-seizure business practices.

TENNECO'S CHIEF TAKES A POWDER

► Under fire from angry investors, Tenneco Chairman James Ketelsen will take early retirement next year, ending

a tumultuous 14-year reign. Ketelsen, 60, will step down as CEO in January and as chairman in May, and he will be replaced by Michael Walsh, formerly chairman of Union Pacific RR. While the company denies it, analysts and former executives believe Ketelsen was pushed out by his board after years of red ink at Tenneco's farm- and construction equipment unit, J. I. Case.

Walsh will have his hands full with Case, which suffered a first-half operating loss of \$303 million. Still, the market cheered the personnel change. Tenneco stock jumped 3 1/4% on the news, to 39%.

\$300 MILLION WORTH OF HUMILITY

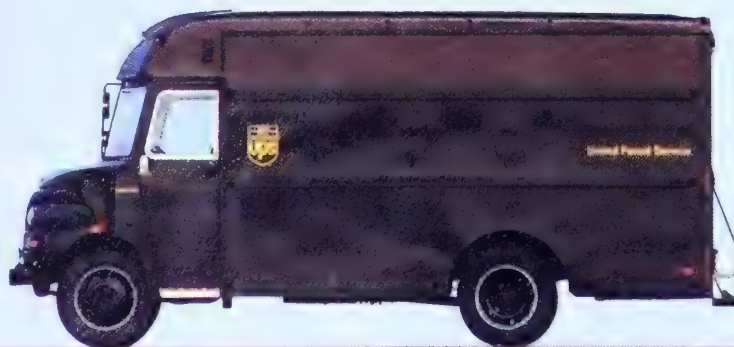
► Finally laying his last and worst deal to rest, financier Bill Farley ceded ownership control of textile maker West Point-Pepperell to creditors. The deal gives banks 10% and bondholders 85% of WP Holdings, which will in turn own 95% of West Point. The stake for Farley and West Point managers: 5%.

Farley calls the outcome "a great lesson in humility. How would you like to go lose \$300 million? Don't you think that would be humbling?"





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Nuclear energy means cleaner air.

SO FAR, THE DEMOCRATIC HOPEFULS LOOK PRETTY HOPELESS

Not so long ago, former South Dakota Senator George S. McGovern was giving Democratic pols anxiety attacks by hinting at another run for the White House. For a few trips to the hustings, wisdom prevailed over ty, and McGovern, who won only Massachusetts and the District of Columbia in his 1972 bid for the Presidency, withdrew from contention. Now, party strategists have something more worrisome to contemplate: With established Democrats abandoning the Presidential field in droves, could the election turn into another McGovernesque disaster?

Maybe. News that West Virginia Governor John D. Rockefeller IV has decided against seeking the nomination after months of testing the waters has left Democratic leaders uneasy—and assessing two distinctly different choices:

Paul E. Tsongas, who is running as a “probusiness liberal,” has ignited new sparks thus far with his diatribes on industrial policy. The former Massachusetts senator is having trouble raising money.

Meanwhile Senator Tom Harkin, who is getting closer to a declaration of candidacy, at least moves the charisma

over a few ticks with his fist-pounding oratory. But Harkin's class-based attacks on “George Herbert Walker Bush” and his throwback populism make the Iowan an unlikely choice to win over the middle class. “Harkin can match [New York Governor] Mario Cuomo emotion for emotion,” says Democratic strategist Mark Siegel. But, adds Robert J. Shafer of the centrist Progressive Policy Institute, “if Harkin finds Democratic policies that didn't work, he'll lose big.” Still weighing the race are several Southerners more to the right of party moderates. Tennessee Senator Albert Gore Jr. mounted an abortive '88 run but is ambivalent about another run against a popular incumbent. Arkansas Governor Bill Clinton

has been hobbled by a home-state pledge to pass up '92—and hurt by a whispering campaign about his personal life—but may jump in soon. Then there's L. Douglas Wilder, Virginia's high-profile governor. A fiscal conservative, Wilder has authorized an exploratory committee and is stepping up his critiques of liberal orthodoxy. But Wilder has harmed his chances by getting drawn into a Dixie mud-fest with fellow Virginian and Democrat Senator Charles S. Robb, an old foe.

SITTING IT OUT. The list of heavyweights who have opted out of the Presidential sweepstakes is a telling indication of how

tough pollsters think '92 will be. Besides Rockefeller, House Majority Leader Richard A. Gephardt (D-Mo.) has decided to sit it out. Cuomo still denies any interest, but maintains a candidate's schedule. And Texan Lloyd Bentsen has brushed aside suggestions that he cap his Senate career with a go at Bush.

Hill Democrats are already blanching at the implications of a minor figure capturing the nomination. “Some of us are starting to worry about the vacuum at the top,” says a senior party official. “It could hurt the rest of the ticket.”



HARKIN: BUSH-BASHING AND THROWBACK POPULISM

One nightmare scenario: A Bush-bashing Harkin wins the Iowa caucuses handily. His momentum leads to a strong showing in New Hampshire, where a Southern challenge fizzles. Meanwhile, Tsongas continues to send voters to Tslumberland, allowing Harkin—backed by Big Labor—to surge in the big industrial-state contests. Harkin rolls up the nomination, campaigning on a promise of huge defense cuts, soak-the-rich taxes, business bashing, and massive antipoverty programs. The result: a fall debacle that drags down scores of congressional Democrats and costs the party control of the Senate.

But that couldn't happen in '92. Or could it?

By Lee Walczak, with Paula Dwyer

CRITICAL WRAPUP

HEALTH CARE

A coalition of unions, health care groups, and more than two dozen large corporations is considering deepening health care reform that would call for government price controls on doctors' fees and hospital charges. An early draft of a proposal from the National Leadership Coalition

Health Care Reform, which includes such major employers as Chrysler, Southern California Edison, and Bethlehem Steel, also recommends a universal health care system that would provide insurance benefits to all Americans. Under the plan, which is scheduled for release in October, states

would set fee schedules for both public and private buyers of health care and establish an overall spending target for medical care. Fee hikes would slow if the spending targets were exceeded.

TAXES

Charities are furious about proposed IRS rules that would limit companies' ability to write off contributions against U.S. income. Under the rules, if a donation goes overseas to help, say, flood victims in Bangladesh, the deduction could be used to offset only foreign-source income. Charities claim that since big corporate givers already have excess foreign tax credits, the rules would reduce corporate giving.

BCCI

Democrats may try to tar the Bush Administration with the Bank of Commerce & Credit International mess, but the White House isn't blinking yet. FDIC Chairman L. William Seidman recently announced that he would retire on Oct. 16, and the Administration seems inclined to nominate as his successor William Taylor—a Federal Reserve senior bank regulator at a time when the Fed failed to detect that BCCI illegally owned a Washington bank. Nor is Bush wavering on nominee Robert M. Gates to head the CIA, which had links to BCCI while Gates was a top agency official.

A TEST OF FIRE FOR A SAMURAI

Can scandal-snared Finance Minister Ryutaro Hashimoto beat the heat again?

With the flourish of samurai politics, powerful Finance Minister Ryutaro Hashimoto offered last month to make a "beautiful exit" and resign to put an end to Japan's snowballing financial scandals. "Cutting my neck," he told power brokers in the ruling Liberal Democratic Party, "would be the cleanest way to go." They appealed to his fighter instincts to stay on.

But now, as scandals involving Japan's brokers and bankers start to claim political victims, Hashimoto is feeling the cold metal against his neck. Once considered a strong contender to become Prime Minister this fall, the 54-year-old Hashimoto is facing the fiercest battle of his stormy career. A report in a Japanese newspaper has linked him with an unsavory deal to funnel loans to several of his acquaintances. Smacking of the same kind of favoritism for which Hashimoto blasted mighty Nomura Securities Co. and other brokers, the revelation has dashed his chances of becoming the next Prime Minister. The issue is whether Hashimoto can cling to power at the Finance Ministry.

Not one to back down from a fight, Hashimoto is resisting calls by the opposition party to resign. Making a beautiful exit and quietly rebuilding alliances with LDP power brokers is not Hashimoto's style. He is cut from a different cloth than many of the consensus-minded players in Nagatacho, Tokyo's political district. Hashimoto is consistently ranked as one of Japan's most popular politicians, and he has been able to cash in on his good looks and sense of dra-



IN ANY LANGUAGE, NO COMMENT: HASHIMOTO AT A WASHINGTON RECEPTION

ma to ease through tight spots. If he plays the scandal right, he could transform disaster into opportunity—and catapult his career even higher.

Fiery temper and all, Hashimoto is a good example of a new generation of more cosmopolitan but tough-minded politicians, less inclined to toe the U.S. line. They were all born after 1925, when the late Emperor Hirohito ascended the throne. Hashimoto and his peers share views shaped by the

prosperous postwar years and conditioned by Japan's growing independence. While older politicians are more respectful of U.S. generosity, men of Hashimoto's age don't exhibit the same sense of indebtedness.

He's also a doer. While many Japanese politicians are content to maneuver in the shadows, Hashimoto wishes his role on the front line. The LDP leadership has singled him out at different points in his career to deal with thorny issues. When others ran for cover, Hashimoto helped to privatize the railroads and push through a bitterly controversial tax on consumer goods. Even if Hashimoto resigns, Japanese politics repeatedly proves that there is life after scandals. With at least another 10 years to maneuver to become Prime Minister, Hashimoto is a man to watch.

BELLWETHER. But it won't be easy to tough this scandal out. Hashimoto faced weeks of grueling investigations by the Diet into the scandals and into the ministry's and his personal role in policing the industry. Already, he is showing some signs of strain, telling colleagues that this ordeal was like "sitting on a bed of

nails." The daily newspaper *Yomiuri Shimbun* reported on Aug. 6 that he would resign by the end of the month, which the LDP promptly denied. Hashimoto declined an interview.

If Hashimoto goes, Japanese politics will undoubtedly experience a far-ranging shake-up. For starters, his resignation would deal a major blow to Prime Minister Toshiki Kaifu. Although largely powerless as a leader, Kaifu has been able to survive

is Mr. Clean image. One reason is that Hashimoto has borne the brunt of the attacks by the opposition and the media on ministry's failure to root out financial crises. As far as Kaifu is concerned, Hashimoto is equipped to take the heat. But resignation would expose Kaifu to the fury of the Diet and make it more difficult to maintain his Teflon image. "If Hashimoto resigns, the next to go will be me," predicts Yasunori Sone, a politics professor at Keio University.

Such upheaval would also frustrate Bush Administration's efforts to improve relations with Tokyo. Having stakingly cultivated Kaifu for two years, White House officials hope he will implement needed trade and political reforms. During a special session of Diet, Kaifu is backing reform bills that would redraw political districts, impose stricter guidelines on campaign gifts. But first, he needs Hashimoto to press ahead with legislation to allow compensation payments for market losses and to reorganize ministry's enforcement division.

As Foreign Minister, Hashimoto is a player in U.S.-Japanese relations in his right. He's at the center of action on such issues as debt forgiveness for Poland and Operation Desert Storm compensation, financial-market liberalization, and aid to developing nations. Although Hashimoto has on occasion sparred with Treasury Secretary Nicholas F. Brady, his U.S. counterpart, Brady has publicly lobbied on Hashimoto's behalf.

When the stock market scandal first broke two months ago, few, in fact, thought the trail would ever lead to Hashimoto. All eyes were on the Finance Minister to lead the charge in kicking down on Japan's brokers for reimbursing big clients for roughly \$1 billion in losses. But in one of the twists for which Japanese politics is famous, Hashimoto suddenly became a suspect.

Y LOANS. In a story broken by the *Yomiuri Shimbun* on Aug. 3, Hashimoto's top aide, Toyoki Kobayashi, said to have used his influence to arrange loans for three people with close links to Hashimoto (table). The money went to a popular actor, an owner of a tempura restaurant, and a developer of sports facilities. Kobayashi promptly resigned. Standing next to Hashimoto at a press conference, Kobayashi accepted blame. But that argument is hardly convincing. On July 25, Kobayashi had resigned the incident to Hashimoto. The Finance Minister reportedly reprimanded him for not being more careful. But Hashimoto did not make a public disclosure.

Even before this, his handling of the stock market scandal had come under attack. It took him three weeks to levy any

discipline on the brokers. Few were impressed by his decision to cut his \$120,000 salary by 10% for three months. And his repeated efforts to quash any form of a U.S.-style Securities & Exchange Commission so as to preserve the wide powers of the Finance Ministry cast doubt on his reputation as an independent thinker.

More dirt could fly before this scandal ends. But if anyone has good survival instincts, it's Hashimoto. In 1986, then-Prime

Minister Hashimoto took to the road to pump flesh. His 10,000-mile charm offensive wasn't enough to save the LDP in July, 1989, elections, but it helped contain the damage.

Soon after, his rivals inside the LDP maneuvered him into becoming Finance Minister, where he faced widespread anger from Japanese consumers over a 3% consumption tax. In the logic of Nagata-cho, he was set up for a fall. Hashimoto not only survived, he turned the issue around. Taking advantage of his popularity with the voters, he took out newspaper ads to make a personal appeal to accept the tax. Public opposition faded.

Although he has proved useful in the hot seat, Hashimoto has not garnered much support within the LDP. Colleagues describe him as swift and energetic, even brilliant, but they're put off by his argumentative, albeit cool, style. More like a British member of Parliament, Hashimoto spars during Diet sessions with opponents. Along the way, he has bruised plenty of egos. "That approach doesn't work here in Nagata-cho," complains one senior LDP member. Even in his own faction in the LDP, headed by former Prime Minister Noboru Takeshita, Hashimoto has few followers.

SHOUTING MATCH. To a degree, Hashimoto is stepping in his father's footsteps. Branded as a troublemaker, Ryogo Hashimoto, a member of Japan's Cabinet during the U.S. occupation after World War II, first won a seat in the Diet in 1949 and soon earned the antipathy of bureaucrats for his inflexible—and often principled—ways. He even quit his job as Health Minister when Finance Ministry officials refused to increase welfare payments to Japanese war victims.

While equally outspoken, the younger Hashimoto has strayed from his father's maxim to defend the weak. In 1969, as a young assistant to the Health & Welfare Minister, he got into a shouting match with victims seeking greater compensation in one of Japan's worst cases of industrial poisoning. When colleagues intervened, Hashimoto roared at them to be silent. Embarrassed aides scurried around bearing gifts of sake to apologize to Hashimoto's supporters.

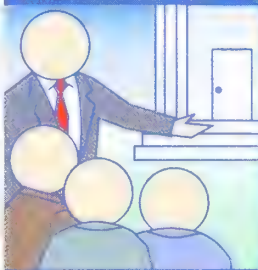
Hashimoto has become much more polished since then. Even so, his career is in limbo as he weathers his first scandal. Meanwhile, the rest of the world is demanding a new brand of leadership from Japan. But the Finance Minister's plight and the series of scandals rocking Nagata-cho mean that will just have to wait.

By Ted Holden in Tokyo, with Paul Magnusson in Washington and Joyce Barnathan in New York

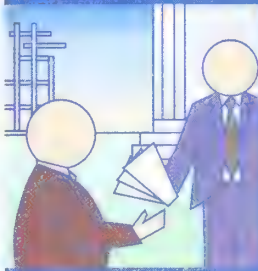
THE SCANDAL THAT MAY TRIP HASHIMOTO



Secretary Toyoki Kobayashi is a longtime fund-raiser for Finance Minister Hashimoto



Kobayashi says he introduced three Hashimoto associates to a Fuji Bank manager. One ran a restaurant, another was building an amusement park and a third an athletic club



To indirectly provide Hashimoto's associates with funds, the Fuji Bank manager issued fake certificates of deposit to a developer, also a political contributor to Hashimoto



The developer allegedly used the fake certificates as collateral to obtain loans from finance companies. The money went to Hashimoto's friends for their projects

Minister Yasuhiro Nakasone put Hashimoto in charge of the Transportation Ministry just as it went ahead with a controversial plan to privatize the national railway system. Faced with bitter opposition from Japan's unions, Hashimoto managed to get the plan through.

Tainted by the Recruit Co. scandal, the LDP again tapped into Hashimoto's popularity and named him secretary general of the party. With the goal of drumming up

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Marketing Manager
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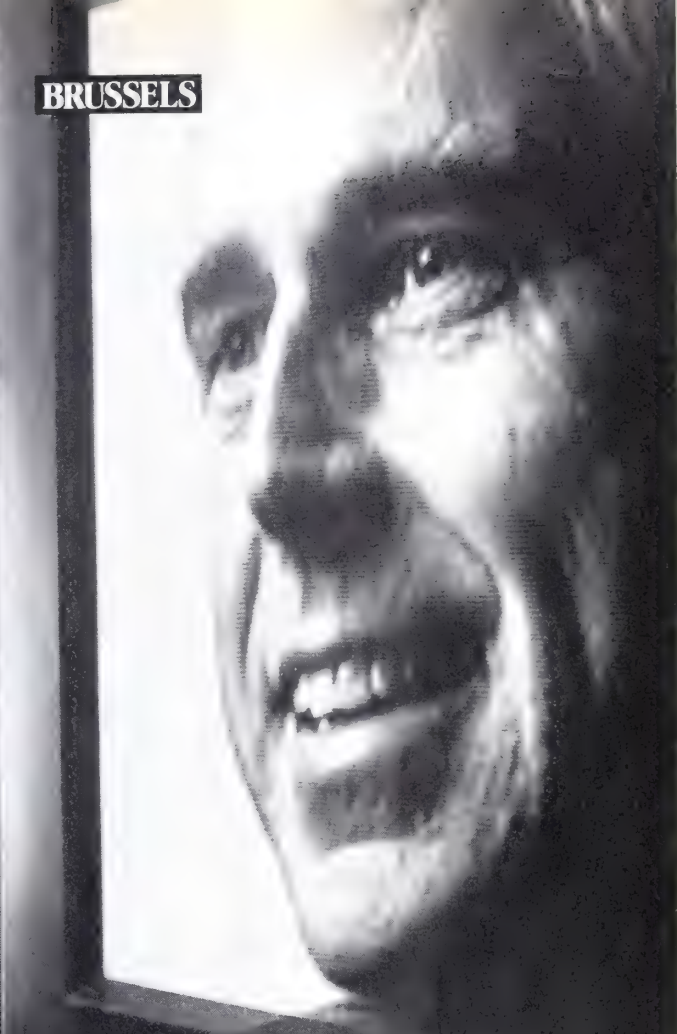
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CAN THE RECOVERY SURVIVE

EXPECTATIONS FOR THE QUARTER WERE LOW, BUT PROFITS—DOWN 23%

By the official reckoning, the recession may have come to an end in the second quarter. But the decline in corporate profits was so sharp that some economists say it could pose a threat to the recovery. Although the anemic 0.4% gain in second-quarter gross national product reported by the Commerce Dept. was below expectations, it wasn't such a surprise as the drop in earnings. According to Standard & Poor's Compustat Services Inc., profits for the 900 companies in BUSINESS WEEK's Corporate Scoreboard fell 23% compared with last year's second quarter. That's much worse than the 10% decline that some analysts had been projecting as recently as two weeks ago.

What went wrong? Some companies in the hard-hit technology sector unexpectedly took massive charges to cover the costs of restructuring their operations. If the office equipment and computer group had been excluded from the Scoreboard, the decrease in earnings would have been only 16%.

Losses at the Big Three auto makers also dragged profits down. If the automotive companies had been left out, the decline also would have been just 16%. Without autos or computers, earnings would have been off 8%—about what many analysts had been predicting.

FEWER SURPRISES. But when all the numbers are factored in, the 23% drop in profits was the largest since corporate earnings began their slide in the third quarter of 1989. Sales were extraordinarily weak, too. They inched ahead just 2% in the quarter, also the poorest performance since the downturn in profits began. For the first half of 1991, profits fell 17%, and sales grew 3%.

If economists were caught off guard by the weakness in corporate profits as a whole, most industry analysts were apparently braced for the lackluster results. The second quarter brought fewer individual earnings "surprises"—results significantly higher or lower than analysts' projections—than usual. In the previous three quarters, 14% of corporate earnings were surprisingly higher than industry analysts were expecting, while 45% were lower, says Thomas Doerflinger, an economist with Paine-Webber Inc. In the latest quarter, he

says that 16% of the earnings reports were considered good surprises while 33% qualified as bad surprises. "The reason second-quarter earnings did not seem disastrous is that expectations have been driven through the floor," says Doerflinger.

And if profits fail to bounce back as

fast as companies and Wall Street expecting them to, there is the danger that the recovery could be short-lived. That's because businesses have little incentive to expand production and hire more workers unless they are getting adequate return on their investment. If we don't get the big profit gains this



WINNERS AND LOSERS

THE INDUSTRIES

THE SHARPEST GAINS THE DEEPEST DROPS

	Percent change from 1990's second quarter	Percent change from 1990's second quarter
TIRE & RUBBER	140%	COMPUTER & PERIPHERALS
HEALTH CARE SERVICES	63	CARS & TRUCKS
AEROSPACE	58	SAVINGS & LOAN
TOBACCO	42	STEEL
BANKS—MIDWEST	38	AIRLINES
ELECTRIC UTILITIES	31	RAILROADS
INSTRUMENTS	30	AUTO PARTS
RETAILING	27	GAS & TRANSMISSION
FOOD RETAILING	26	BANKS—WEST & SOUTHWEST
DRUGS & RESEARCH	26	FOREST PRODUCTS
FINANCIAL SERVICES	25	MACHINE & HAND TOOLS
GLASS CONTAINERS	21	ALUMINUM
MEDICAL PRODUCTS	16	BUILDING MATERIALS
TELECOMMUNICATION SERVICES	16	CONSTRUCTION & REAL ESTATE
INSURANCE	15	ENTERTAINMENT

ALL-INDUSTRY AVERAGE: -23%

THIS DIVE?

STILL DISAPPOINTED ALMOST EVERYBODY

One has been anticipating, it could still be the economy," says Paul Getman, managing director of Regional Financial Associates Inc., an economic forecasting firm in West Chester, Pa.

Still, most analysts are looking for a rebound in earnings during the second half of the year. "Compared to a year

ago, we're still in a slump," says Kurt Karl, senior economist with WEFA Group Inc. in Philadelphia. "But the economy is improving, and costs are quite low. It looks like it's up from here."

Even a strong second half may not be enough to overcome the shortfall in the first two quarters, however. A few

weeks ago, economists were projecting that 1991 earnings for the companies in the Standard & Poor's 500-stock index would be about even with 1990 results. Now, Doerflinger and others are forecasting a slight decline. Getman expects this rebound to be about half as strong as normal. In the typical recovery, earnings bounce back about 43%. This time, they'll increase just 22%, he says.

NO CUSHION. If the rebound is weak, some blame will go to the strengthening dollar and slower growth overseas. The greenback will be up on a year-over-year basis in the second half of 1991, says Doerflinger, making foreign profits smaller when they're converted into dollars. And while overseas earnings provided a cushion during the latest downturn, foreign economies are starting to stall. That's already hurting the results of computer makers, which until recently had enjoyed strong European growth.

At home, most economists don't see any end to the intense price pressure that began well before the recession started. In the face of restrained inflation and tough competition from foreign producers, it will be difficult for U.S. companies to increase earnings by raising prices. Nowhere is that more apparent than in autos, computers, and steel, where excess capacity has made it hard to earn a buck. All three sectors reported losses during the second quarter.

Without much in the way of sales growth, companies must boost productivity and reduce overhead in order to improve profit margins. That's what's behind the special charges taken in the second quarter by Unisys Corp. and Digital Equipment Corp. Unisys took pretax charges totaling \$1.2 billion, including \$925 million to reduce its work force by 10,000, while Digital took a \$1.1 billion charge to cover the cost of eliminating 10,000 positions. Du Pont, Arco, and Wang Laboratories also took write-offs in the quarter to cut thousands of jobs.

Although car- and truckmakers reported a \$1.34 billion loss, Goodyear Tire & Rubber Co. edged back into the black, helping the tire and rubber companies post the largest gain, 140%, of any group. Goodyear benefited from the lack of a restructuring charge taken in the year-ago quarter, lower selling ex-

SECOND-QUARTER PROFITS

THE COMPANIES

MADE THE MOST		WHO LOST THE MOST	
	Millions of dollars		Millions of dollars
AMERIS	\$1,153	UNISYS	\$1,300
ELECTRIC	1,131	DIGITAL EQUIPMENT	871
	1,125	GENERAL MOTORS	785
	828	BURLINGTON NORTHERN	420
	556	MIDLANTIC	415
	549	FORD MOTOR	324
WATSON SQUIBB	490	WANG LABORATORIES	306
3M	482	CHRYSLER	212
	454	TEXAS INSTRUMENTS	157
	445	GLENFED	137
MORTGAGE ASSN.	418	CROSSLAND SAVINGS	123
& JOHNSON	406	R. H. MACY	116
	403	HOMEFED	113
	384	QUANTUM CHEMICAL	87
WELLS FARGO	365	MNC FINANCIAL	82

DATA: STANDARD & POOR'S COMPUSTAT SERVICES INC.



Corporate Scoreboard

penses, and better results abroad. Other sectors that turned in sharp earnings increases included health care services, up 63%; aerospace, up 58%; tobacco, ahead 42%; and Midwest banks, up 38%.

Philip Morris Cos. earned the most in the second quarter, with \$1.15 billion in profits, ahead 22%. The food-and-tobacco giant was followed by General Electric, which earned \$1.13 billion, up 4%; Exxon,

with \$1.125 billion in profits, up 2%; and American Telephone & Telegraph, which earned \$828 million, up 26%. Attesting to the strength of the health care industry was Merck & Co., where earnings rose 18%, to \$556 million.

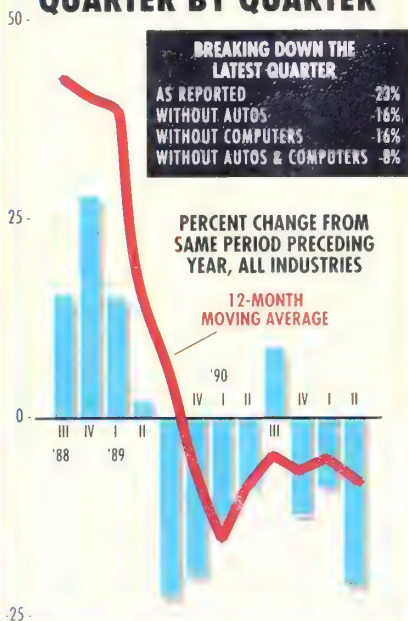
Because of its restructuring, Unisys recorded the biggest loss of any company, \$1.3 billion. It was followed by Digital, whose special charges led to an \$871

million loss. General Motors was next on the list, with a \$785 million loss, followed by Burlington Northern, which lost \$1 million, and Midlantic, down \$415 million. Those results are pretty grim, to sure. But they'll be grimmer still if a weak second quarter undermines budding recovery.

By Monica Roman in New York, and Zachary Schiller in Cleveland

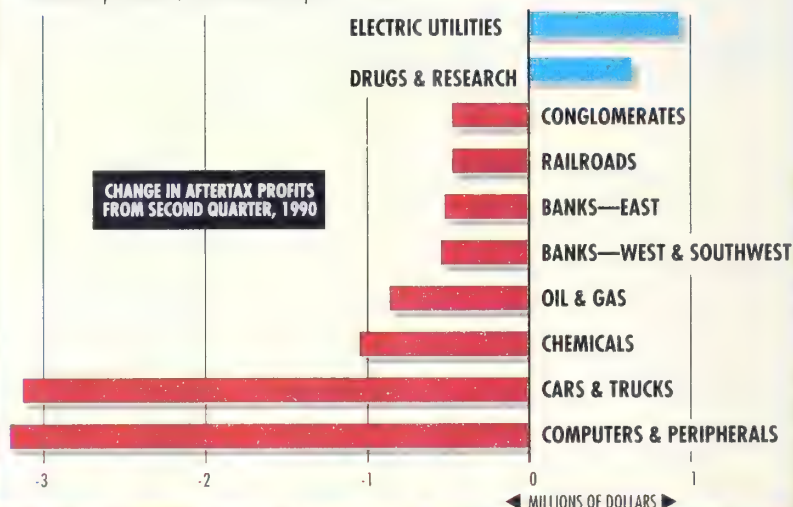
A SPOTLIGHT ON SECOND-QUARTER PROFITS

AFTERTAX PROFITS, QUARTER BY QUARTER

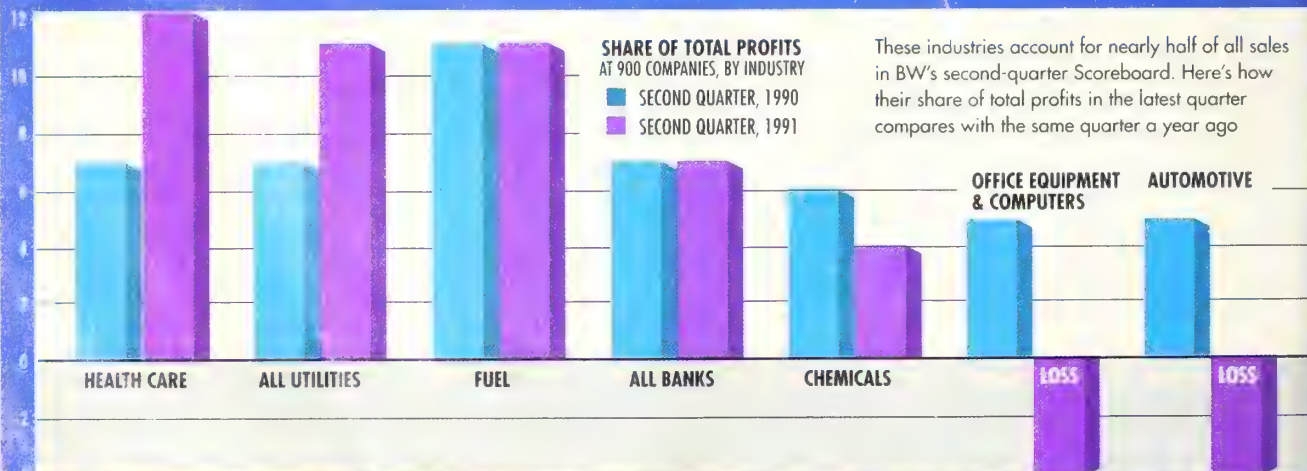


INDUSTRY GROUPS WITH THE BIGGEST DOLLAR CHANGE IN THE QUARTER

How bad was the second quarter? Consider that 41 of the 69 industry groups in the Scoreboard had lower earnings than a year ago. It all adds up to a 23% drop in profits on sales growth of only 2%. Autos and computers contributed almost two-thirds of the second-quarter's \$9.9 billion drop



WHO'S LEADING THE PACK — AND WHO'S LAGGING



These industries account for nearly half of all sales in BW's second-quarter Scoreboard. Here's how their share of total profits in the latest quarter compares with the same quarter a year ago

CORPORATE SCOREBOARD

SECOND QUARTER 1991

SUMMARY

Sales: Includes all sales and other operating revenues. For banks, includes all operating revenues.

Profits: Net income before extraordinary items. For banks, profits are net income after extraordinary gains or losses.

Margins: Net income from continuing operations before extraordinary items as percent of sales.

Return on common equity: Ratio of net income available for common stockholders (most recent 12 months) to latest available common equity, which includes common stock, capital surplus, and retained earnings.

Price-earnings ratio: Based on July 26, 1991, common stock price and corporate earnings from continuing operations before extraordinary items for most recent 12-month period.

Earnings per share: For most recent 12-month period. Includes all common-stock equivalents.

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE- EARNINGS RATIO 7-26	12 MONTHS' EARNINGS PER SHARE
	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 %	2ND QUARTER 1990 %			
AIR-INDUSTRY COMPOSITE	906675.3	2	1812508.0	3	34036.0	-23	71687.8	-17	3.8	5.0	10.3	20	1.90
AEROSPACE													
INDUSTRY COMPOSITE	28364.0	4	52896.6	2	1057.7	58	1743.7	18	3.7	2.5	12.6	11	3.77
Airbus	7813.0	12	13904.0	4	454.0	17	763.0	11	5.8	5.6	20.0	10	4.24
AirCorp (1)	500.0	9	933.0	16	13.0	30	11.0	-67	2.6	2.2	14.5	12	0.91
Boeing	2416.0	-8	4717.0	-8	211.0	NM	268.0	NM	8.7	NM	-12.4	NM	-4.67
Boeing	1009.1**	-4	1890.7	-1	29.6	11	52.1	21	2.9	2.6	10.0	7	2.74
Boeing	2430.0	1	4666.0	0	70.0	-14	124.0	-17	2.9	3.4	13.2	9	4.89
Boeing	1567.8	-5	2968.2	-4	97.9	4	169.0	5	6.2	5.7	19.5	9	6.74
Boeing	5044.0**	22	9367.0	18	77.0	97	135.0	246	1.5	0.9	10.5	6	9.67
Boeing	1325.0	-6	2571.8	-4	36.2	24	75.5	-40	2.7	2.1	15.1	9	3.42
Boeing	358.2	20	659.2	25	9.0	106	14.7	233	2.5	1.5	6.1	16	1.49
Boeing	407.1	4	810.0	4	8.7	-61	32.4	-35	2.1	5.7	15.4	12	2.72
Boeing	117.0**	1	229.3	2	7.9	4	15.4	3	6.8	6.6	14.9	18	1.75
Boeing	5376.9**	-6	10180.4	-3	43.4	-79	83.6	-76	0.8	3.6	8.6	13	3.75
Automotive													
INDUSTRY COMPOSITE	72787.3	-9	137997.9	-9	-1236.6	NM	-3310.3	NM	NM	2.6	-11.7	NM	-4.01
TRUCKS & TRUCKS													
INDUSTRY COMPOSITE	64476.3	-10	122170.4	-9	-1340.4	NM	-3291.8	NM	NM	2.6	-13.1	NM	-5.03
Chrysler	7810.0**	-12	13610.0	-17	-212.0	NM	-553.0	NM	NM	2.0	-11.8	NM	-3.28
Chrysler	23846.7	-11	45187.7	-10	-323.5	NM	-1207.9	NM	NM	2.9	-7.9	NM	-3.45
Chrysler	31328.6**	-8	60515.6	-6	-784.5	NM	-1467.5	NM	NM	2.7	-17.6	NM	-9.15
Chrysler	940.0	-8	1782.0	-7	-29.0	NM	-67.0	NM	NM	0.8	-18.5	NM	-0.39
Chrysler	551.0	-19	1075.2	-22	8.6	-54	3.6	-92	1.6	2.8	2.3	71	0.67
Trucks & Equipment													
INDUSTRY COMPOSITE	5124.4	-6	9810.9	-8	43.4	-75	-14.3	NM	0.8	3.2	-1.3	NM	-0.21
Chrysler	443.3	0	827.0	-2	7.7	-30	6.5	-51	1.7	2.5	5.2	24	1.00
Chrysler	877.6	1	1689.1	-3	-17.2	NM	-51.5	NM	NM	0.7	-44.5	NM	-16.36
Chrysler	1181.5	-15	2285.7	-16	4.6	-85	6.7	-88	0.4	2.3	2.8	49	0.67
Chrysler	115.3	3	231.2	10	6.2	-14	11.2	0	5.4	6.5	17.5	14	2.43
Chrysler	155.0	-16	293.3	-17	-2.4	NM	-5.8	NM	NM	12.3	NM	4	0.48
Chrysler	855.0	-10	1673.0	-12	27.0	-46	13.0	-87	3.2	5.3	7.5	28	2.36
Chrysler	438.9	3	836.7	4	11.3	-17	18.4	-9	2.6	3.2	6.4	17	0.78
Chrysler	365.7	-13	680.9	-16	-0.5	NM	-9.7	NM	NM	2.3	-14.9	NM	-0.75
Chrysler	125.9	10	248.4	11	6.5	-3	8.5	-38	5.1	5.9	14.8	11	2.02
Chrysler	242.6	-9	442.6	-12	1.7	-87	0.8	-95	0.7	4.7	3.7	15	1.30
Chrysler	151.3	15	281.2	8	3.9	203	5.9	39	2.6	1.0	6.1	17	0.72
Chrysler	172.2	8	321.9	2	-5.3	NM	-18.3	NM	NM	2.8	-15.6	NM	-2.06
Tire & Rubber													
INDUSTRY COMPOSITE	3186.7	-2	6016.6	-4	60.4	140	-4.3	NM	1.9	0.8	1.2	NM	0.27
Goodyear	145.1	2	270.2	0	18.4	-2	31.5	-9	12.7	13.2	30.0	19	5.39
Goodyear	250.3	7	458.1	3	19.5	19	31.8	6	7.8	7.0	17.2	18	1.65
Goodyear	2791.3	-3	5288.3	-5	22.5	NM	-67.6	NM	0.8	NM	-5.9	NM	-1.93

Second quarter ending May 31. (2) Second quarter ending Apr. 30. (3) Third quarter and most recent six months ending June 30. (4) Third quarter and most recent six months ending May 31. (5) Third quarter and most recent six months ending Apr. 30. (6) Fourth quarter and most recent six months ending June 30. (7) Fourth quarter and most recent six months ending May 31. (8) Fourth quarter and most recent six months ending Apr. 30. (9) First quarter and most recent six months ending June 30. (10) First quarter and most recent six months ending May 31. (11) First quarter and most recent six months ending Apr. 30. *Sales include excise taxes. **Sales include other income. ***Sales include excise taxes and other income. †Revenues from subsidiaries not included in consolidated sales. Earnings per share are for latest 12 months, not necessarily for end of most recent fiscal year; they include all common stock equivalents and exclude extraordinary items. NA=not available. NM=not meaningful.

DATA: STANDARD & POOR'S COMPUSTAT SERVICES INC.

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS				RETURN ON COMMON EQUITY 10 MONTHS ENDING 6/30	PRICE EARNINGS RATIO 7/26	MOON EARN PER SH.
	END QUARTER 1991 \$ MIL.	CHANGE FROM 90 %	10 MONTHS 1991 \$ MIL.	CHANGE FROM 90 %	END QUARTER 90 \$ MIL.	CHANGE FROM 90 %	5 MONTHS 1991 \$ MIL.	CHANGE FROM 90 %	END QUARTER 1991 %	END QUARTER 1990 %	END QUARTER 1990 %				
3 BANKS															
INDUSTRY COMPOSITE	48847.1	-7	99932.1	-6	2218.7	-29	5057.1	-22	4.5	5.9	5.6	20	1.4		
BANKS - EAST															
GROUP COMPOSITE	23991.2	-10	49537.2	-9	680.6	-43	1782.4	-30	2.8	4.4	0.8	NM	0.2		
Bank of Boston	1038.0	-15	2114.7	-32	-49.5	NM	-145.9	NM	NM	0.1	-47.5	NM	-8.7		
Bank of New York	1035.9	-24	2204.6	-18	60.6	-14	-2.7	NM	5.8	5.2	4.1	21	1.4		
Bankers Trust New York	1700.0	-14	3545.0	-12	185.0	6	345.0	-7	10.9	8.8	23.1	8	7.3		
Chase Manhattan	2879.0	-12	5975.0	-15	131.0	52	248.0	158	4.6	1.6	-6.7	NM	-2.2		
Chemical Banking	1734.5	-11	3515.4	-13	94.0	-17	181.0	-32	5.4	5.8	4.3	19	1.3		
Citicorp	3744.0	5	7269.0	3	43.0	-83	113.0	-76	1.1	6.9	-2.6	NM	-0.6		
CoreStates Financial	601.1	-6	1225.3	-4	56.0	-10	106.8	-14	9.3	9.8	6.9	23	1.7		
First Fidelity Bancorporation	678.5	-10	1415.4	-7	52.0	NM	108.1	NM	7.7	NM	15.5	8	3.6		
Fleet/Norstar Financial Group	925.5	NM	1849.6	-13	27.9	-48	53.4	NM	3.0	5.2	1.4	63	0.3		
KeyCorp	557.2	30	1064.0	27	44.0	18	82.9	13	7.9	8.7	2.9	10	3.5		
Manufacturers Hanover	669.0	-11	3528.0	-8	75.0	127	153.0	19	4.5	1.7	3.8	20	1.4		
Mellon Bank	777.0	-20	1574.0	-13	70.0	-51	138.0	-33	9.0	4.7	3.7	26	1.2		
Meridian Bancorp	338.4	8	606.8	1	36.6	57	56.9	14	10.8	7.5	8.0	13	1.3		
Midlantic	500.8	-27	1041.5	-20	-415.3	NM	-438.1	NM	NM	NM	-51.2	NM	-16.0		
MNC Financial	440.7	-45	1041.5	-16	-82.3	NM	71.7	NM	NM	NM	-24.7	NM	-3.5		
Morgan (J. P.)	2407.0	-8	5104.0	-1	231.0	12	504.0	34	9.6	7.9	17.3	11	4.6		
PNC Financial	1122.3	-9	2287.0	-8	93.6	-14	182.0	-1	8.3	8.8	2.4	56	0.6		
Republic New York	589.0	-6	1311.6	10	56.4	7	111.1	14	8.9	7.8	3.6	12	5.8		
Shawmut National	559.1	-16	1208.1	-14	-58.7	NM	-175.4	NM	NM	3.8	-35.2	NM	-5.0		
State Street Boston	319.8	-1	697.6	11	26.3	-8	83.8	49	8.2	8.8	19.4	12	3.9		
UJB Financial	311.8	-3	629.3	-1	4.0	-37	5.9	-81	1.3	2.0	-4.2	NM	-0.7		
BANKS - MIDWEST															
GROUP COMPOSITE	8534.7	-5	17310.8	-4	756.8	38	1441.0	20	8.9	6.1	11.7	11	2.9		
Ameritrust	588.4	-10	570.8	-7	14.6	-21	26.2	NM	5.1	5.8	-7.4	NM	-1.1		
Banc One	900.9	9	1857.3	12	130.5	26	251.2	22	14.2	12.3	15.7	14	2.9		
Boatmen's Bancshares	389.3	4	793.2	7	37.6	14	72.3	10	9.7	8.8	10.9	11	4.0		
Comerica	346.2	2	701.5	4	37.8	9	73.2	7	10.9	10.2	16.2	7	5.0		
Continental Bank	588.0	-21	1218.0	-26	31.0	NM	62.0	297	5.3	NM	7.7	8	1.7		
First Bank System	447.0	-17	914.2	-17	45.3	52	86.0	48	10.1	5.5	12.5	11	1.7		
First Chicago	1216.0	-14	2483.5	-13	57.3	-34	106.8	-32	4.7	6.2	6.9	10	2.5		
First of America Bank	357.9	7	714.4	7	33.8	7	62.6	-3	9.4	9.4	13.6	9	3.3		
Huntington Bancshares	308.7	-3	611.3	-2	29.6	6	55.2	-1	9.6	8.8	10.6	12	1.4		
Manufacturers National	290.1	1	593.6	6	29.8	10	57.3	17	10.2	9.4	15.3	8	7.5		
Michigan National	272.5	-13	551.6	-10	10.8	-37	13.2	-54	4.0	5.5	3.3	19	1.6		
National City	549.0	-3	1018.2	-2	56.0	-17	107.4	-19	8.6	10.1	12.5	11	3.4		
NBD Bancorp	548.9	-3	1008.7	-1	69.9	3	135.8	1	10.8	10.2	14.5	10	3.7		
Northern Trust	314.6	-4	642.2	1	32.1	18	63.1	16	10.2	8.7	18.9	13	3.3		
Norwest	1091.0	5	2009.8	9	98.0	NM	185.5	249	9.0	NM	11.7	8	3.7		
Society	404.3	-4	813.6	-4	42.5	7	83.0	3	10.5	9.5	15.7	10	4.7		
BANKS - SOUTH & SOUTHEAST															
GROUP COMPOSITE	7056.3	-2	14311.2	1	507.4	-9	954.3	-13	7.2	7.8	9.1	14	2.11		
Barnett Banks	808.0	0	1666.7	4	29.2	-50	47.5	-36	3.5	7.1	4.6	27	1.1		
C&S/Sovran	1248.8	-6	2525.3	-3	64.0	-20	94.8	-50	5.1	6.0	4.3	30	0.89		
Crestar Financial	325.5	4	630.7	3	12.2	36	24.2	-33	3.7	2.9	6.3	16	1.48		
Dominion Bankshares	134.5	-8	517.4	-6	5.7	-72	11.3	76	2.3	7.3	-6.1	NM	-0.89		
First Union	997.3	-3	2038.5	2	73.6	-15	154.5	-6	7.4	8.5	9.9	10	2.4		
NCNB	1644.5	2	3347.5	4	142.2	3	270.6	-2	8.6	8.6	11.1	11	3.22		
Signet Banking	303.2	-13	645.3	-9	8.4	187	14.8	-51	2.8	0.8	3.5	19	0.98		
SunTrust Banks	853.2	1	1706.6	1	92.6	5	181.6	3	10.9	10.5	15.0	11	2.75		
Wachovia	609.8	-3	1233.3	0	79.5	6	155.1	6	10.0	12.0	15.5	12	4.36		
BANKS - WEST & SOUTHWEST															
GROUP COMPOSITE	9264.9	-5	18772.9	-3	273.9	-67	879.5	-47	3.0	8.5	7.5	14	2.39		
Bancorp Hawaii	255.7	14	514.7	18	27.8	21	54.1	19	10.9	10.2	16.0	11	5.75		
BankAmerica	3054.0	1	6167.0	4	272.0	28	554.0	29	8.9	7.0	15.8	8	4.35		
First City Bancorporation of Texas	261.9	-25	558.2	-34	-58.9	NM	-130.1	NM	NM	5.7	-91.7	NM	-22.84		
First Interstate Bancorp	1345.8	-10	2703.6	-10	-80.3	NM	-20.6	NM	NM	6.4	8.0	9	3.08		
Security Pacific	2318.5	-11	4737.6	-7	46.7	-76	143.2	-63	2.0	7.5	-2.8	NM	-1.05		
U. S. Bancorp	279.7	17	549.1	17	42.2	-15	91.5	-2	15.1	20.6	13.8	9	2.97		
Valley National	279.6	-2	556.6	-1	10.4	429	21.4	730	3.7	0.7	5.4	18	1.33		
Wells Fargo	1470.0	-6	2986.0	0	14.0	-94	166.0	-58	1.0	14.9	15.3	8	9.01		
4 CHEMICALS															
INDUSTRY COMPOSITE	34776.9	1	69380.1	2	1518.4	-41	3637.0	-27	4.4	7.5	13.0	16	2.57		
Air Products & Chemicals	773.4	0	1468.1	3	64.1	13	129.9	11	9.0	8.0	14.5	14	4.55		
American Cyanamid	1420.4	16	2733.2	15	131.8	22	236.6	15	9.3	8.8	5.3	42	1.54		
Arco Chemical	703.0	0	1385.0	0	33.0	-68	85.0	-54	4.7	14.5	12.8	18	2.18		
Betz Laboratories	166.3	13	329.7	13	18.8	15	37.1	17	11.3	11.1	27.6	24	2.30		
Cabot	347.2	-12	758.0	-5	6.4	-60	22.0	47	1.9	4.1	11.9	16	1.85		

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE- EARNINGS RATIO 7-26	12 MONTHS' EARNINGS PER SHARE
	2ND QUARTER 1991	CHANGE FROM 1990	6 MONTHS 1991	CHANGE FROM 1990	2ND QUARTER 1991	CHANGE FROM 1990	6 MONTHS 1991	CHANGE FROM 1990	2ND QUARTER 1991	2ND QUARTER 1990			
	\$ MIL	%	\$ MIL	%	\$ MIL	%	\$ MIL	%	%	%			
Compton & Knowles	119.0	21	225.2	17	10.7	22	18.9	20	9.0	9.0	27.0	23	1.35
Interxter	238.0	6	473.0	5	4.8	-60	11.7	-47	2.0	5.4	9.4	16	1.32
Dow Chemical	4794.0**	0	9742.0	0	233.0	-36	811.0	-2	4.9	7.6	15.0	11	5.04
Pont	9825.0***	2	19504.0	2	549.0	-21	1139.0	-13	5.6	7.2	12.9	15	3.17
Gelhard	649.2**	-14	1277.9	-9	22.9	26	44.0	34	3.5	2.4	11.5	17	1.82
Lylyl	638.1	6	1292.0	7	50.1	-12	103.0	-6	7.9	9.5	20.9	13	1.90
Pro	270.1	-4	533.0	-5	-21.8	NM	-19.0	NM	NM	2.5	-6.8	NM	-0.84
St Mississippi (6)	152.2	4	283.4	8	0.5	-31	2.4	14	0.4	0.5	2.8	39	0.27
Report McMoran	390.0	3	796.7	3	27.7	-42	61.7	-77	7.1	12.5	17.8	23	1.64
ler (H. B.) (1)	216.3	6	418.4	8	7.1	10	10.8	61	3.3	3.2	12.4	15	2.75
orgia Gulf	214.1	-2	449.6	-4	16.6	6	33.7	-36	7.8	7.2	NM	10	2.22
odrich (B. F.)	637.0	1	1214.7	-1	8.3	-76	5.4	-89	1.3	5.5	5.0	18	2.43
ace (W. R.)	1707.0	5	3350.0	7	57.6	12	88.4	5	3.4	3.2	11.1	15	2.40
at American Management (5)	484.7	-23	896.2	-19	1.7	-89	-9.1	NM	0.4	2.6	2.4	NM	0.03
at Lakes Chemical	346.1	35	665.3	31	40.0	16	78.6	14	11.6	13.5	19.8	19	4.28
na (M. A.)	277.6	-4	535.4	-4	10.8	-40	16.1	-26	3.9	6.3	8.9	13	1.86
C Fertilizer Group (6)	302.6	-1	588.7	0	29.3	23	47.9	18	9.7	7.8	14.7	13	3.85
ite	141.0	1	279.4	2	18.8	7	34.6	4	13.4	12.6	22.1	20	1.89
orizol	372.3	4	746.7	4	27.6	-17	62.9	1	7.4	9.2	25.6	8	5.46
ondell Petrochemical	1458.0	4	3082.0	7	69.0	-55	168.0	-28	4.7	11.0	210.9	6	3.64
onsanto	2473.0	4	4696.0	1	-52.0	NM	114.0	-74	NM	10.4	5.3	42	1.75
orton International (6)	465.5	8	983.2	12	34.2	-6	74.5	-1	7.3	8.5	12.8	19	2.85
lco Chemical	346.9	18	639.1	12	34.3	4	65.7	5	9.9	11.3	45.1	16	1.76
Industries	217.2	-6	442.2	-4	17.6	-57	-21.8	NM	8.1	17.7	3.0	NM	0.09
n	568.0	-14	1129.0	-13	21.0	-28	-38.0	NM	3.7	4.4	-4.2	NM	-1.20
antum Chemical	582.5*	-1	1322.7	4	-87.1	NM	-67.6	NM	NM	1.2	NM	NM	-2.05
xene	112.4	-3	243.2	-1	-10.4	NM	-21.7	NM	NM	0.9	NM	NM	-0.65
hm & Haas	752.9	-2	1432.6	-2	52.8	-25	94.1	-24	7.0	9.1	14.0	17	2.65
ulman (A.) (4)	177.8	-2	372.1	9	9.7	1	19.6	11	5.5	5.3	18.2	17	2.03
rling Chemicals (3)	110.2	-21	257.4	0	2.5	-87	9.6	-68	2.3	13.5	52.5	5	1.06
ion Carbide	1751.0	-7	3608.0	-5	50.0	-57	133.0	-37	2.9	6.2	9.3	12	1.66
ellman	215.8	3	407.4	-3	11.8	-36	22.1	-39	5.5	8.8	12.0	16	1.46
tco	421.3	4	819.6	3	16.0	-31	32.8	-13	3.8	5.8	10.6	14	2.78
CONGLOMERATES													
INDUSTRY COMPOSITE	43256.7	0	83907.3	0	1927.6	-20	3517.0	-20	4.5	5.6	15.3	15	2.91
Co Standard (3)	1186.0**	3	2416.4	3	23.6	4	45.0	-7	2.0	2.0	11.5	17	1.94
ied-Signal	3047.0	-4	5950.0	-5	89.0	-26	152.0	-39	2.9	3.8	10.6	14	2.68
rt Group (11)	267.5**	12	569.9	10	-0.6	NM	-0.5	NM	NM	1.0	1.9	23	2.80
al	929.8	2	1832.5	3	39.6	1	57.1	2	4.3	4.3	11.3	13	2.94
igie International	313.9	-8	628.3	-8	6.4	-46	12.8	-47	2.1	3.5	8.1	13	1.64
qua Industries	238.4	-5	449.1	-10	-5.9	NM	-20.6	NM	NM	2.3	-12.2	NM	-2.04
neral Cinema (2)	648.7**	1	1214.8	5	27.2	-9	56.0	12	4.2	4.6	7.1	14	1.60
neral Electric	14601.0	3	27740.0	4	1131.0	4	2130.0	5	7.7	7.7	20.1	15	5.02
neral Host (11)	176.8	6	313.1	5	6.6	19	10.4	-6	3.7	3.3	3.2	28	0.28
l	475.6	-3	913.3	-5	-4.3	NM	-5.7	NM	NM	0.1	-7.7	NM	-1.00
V	5142.0	-1	10141.0	0	206.0	-48	435.0	-33	4.0	7.6	NA	10	5.83
V	1561.2	-2	2989.5	-3	13.4	-83	-32.9	NM	0.9	4.8	NM	NM	-0.95
itional Intergroup (9)	712.4	7	1490.5	-11	2.6	NM	-11.3	NM	0.4	NM	-3.4	NM	-0.68
ll (5)	179.5	19	343.2	20	24.7	23	41.4	23	13.8	13.3	16.2	29	1.30
nn Central	678.3	22	1342.0	29	19.9	-24	43.0	-16	2.9	4.7	5.8	14	1.67
emark International	711.2	6	1361.6	6	27.5	304	36.4	82	3.9	1.0	9.3	13	2.22
ckwell International (3)	2978.0	-5	5968.3	-5	151.4	-12	306.6	-11	5.1	5.5	13.8	11	2.47
ledyne	818.5	-7	1630.9	-5	11.0	-59	26.3	-56	1.3	3.0	6.9	28	0.66
nneco	3506.0	-4	6837.0	-6	-14.0	NM	-13.0	NM	NM	5.7	6.1	24	1.55
xtron	2001.4	1	3909.7	1	74.1	3	140.5	2	3.7	3.6	10.5	10	3.26
W	1980.0	-6	3895.0	-5	24.0	-62	59.0	-51	1.2	3.0	7.7	19	2.40
ilhi	493.8**	2	880.0	-5	50.9	26	27.6	-49	10.3	8.3	13.2	17	0.41
hitman	609.7	5	1091.2	4	23.4	48	22.0	38	3.8	2.7	-10.7	NM	-0.44
CONSUMER PRODUCTS													
INDUSTRY COMPOSITE	50818.2	8	99890.5	10	3303.9	18	5894.1	16	6.5	6.0	20.7	20	1.91
PAREL													
GROUP COMPOSITE	5151.0	8	10414.4	9	216.2	9	484.7	1	4.2	4.1	16.4	16	1.74
own Group (11)	422.3	-4	858.8	-7	3.9	-56	11.7	-40	0.9	2.0	8.1	16	1.57
ystal Brands	169.1	-5	376.9	-5	-39.8	NM	-38.4	NM	NM	NM	-6.6	NM	-1.62
uit of the Loom	468.3	6	817.5	7	36.2	-3	52.1	4	7.7	8.4	18.8	13	1.25
irtmarx (1)	293.3	-3	612.3	-5	-5.9	NM	-7.2	NM	NM	NM	-5.5	NM	-0.78
strument Systems (3)	133.4	7	243.2	4	5.2	65	6.7	44	3.9	2.5	17.7	9	0.41
llwood (8)	214.3	12	396.2	9	5.6	NM	6.1	NM	2.6	NM	6.2	20	1.06
A. Gear (1)	182.8	-19	353.7	-14	-4.0	NM	-16.5	NM	NM	4.5	-4.8	NM	-0.48
slie Fay	171.1	3	416.0	7	0.1	-94	10.2	-5	0.0	0.7	14.4	11	1.50
Clairborne	416.0	22	918.1	21	39.5	13	100.5	15	9.5	10.3	28.1	16	2.55
ke (7)	719.0	18	1521.2	28	58.6	-13	129.3	-1	8.2	11.0	28.8	11	3.77

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS				RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE- EARNINGS RATIO 7-26	1 MON EARN PER SH.
	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 %	2ND QUARTER 1990 %					
Oxford Industries (7)	117.2	-14	237.3	-9	1.6	258	3.2	244	1.4	0.3		5.5	20	0.6	
Phillips-Van Heusen (11)	180.4	16	398.8	17	-0.9	NM	4.3	30	NM	0.4		28.6	17	1.7	
Reebok International	688.3	31	1383.6	28	60.4	39	118.8	24	8.8	8.2		19.1	15	1.4	
Russell	167.5	1	319.8	-2	6.3	-51	9.6	-65	3.8	7.7		10.9	22	1.3	
Stride Rite (1)	153.9	8	293.9	10	18.8	19	35.2	19	12.2	11.1		31.4	21	2.3	
VF	654.0	3	1267.3	5	30.7	37	59.2	30	4.7	3.5		11.0	18	1.4	
(b) APPLIANCES & HOME FURNISHINGS															
GROUP COMPOSITE	6415.9	0	12800.2	-2	114.0	-40	156.2	-64	1.8	3.0		1.3	NM	0.1	
Armstrong World Industries	631.3	-3	1230.0	-5	23.4	-54	38.2	-65	3.7	7.9		8.6	21	1.4	
Circuit City Stores (10)	562.2	15	1303.4	10	8.0	-24	34.7	-25	1.4	2.1		14.5	15	1.1	
Heilig-Meyers (10)	124.5**	11	238.7	9	7.4	4	11.4	3	6.0	6.3		8.6	14	2.0	
Highland Superstores (11)	170.1	-8	456.0	-9	-22.4	NM	-20.6	NM	NM	NM		NM	NM	-1.4	
Interco (10)	349.5	-2	694.5	-6	-16.0	NM	-71.8	NM	NM	NM		NM	NM	-5.2	
La-Z-Boy Chair (8)	165.9	-2	317.8	1	8.4	-24	14.5	-16	5.1	6.5		10.2	17	1.3	
Ladd Furniture	113.8	-16	224.6	-18	0.4	-89	-0.6	NM	0.3	2.6		-5.0	NM	-0.3	
Leggett & Platt	282.9	2	546.0	0	9.7	-25	17.3	-32	3.4	4.7		7.0	26	1.2	
Masco	778.0	-6	1531.0	-6	24.9	-60	41.7	-68	3.2	7.5		2.8	65	0.3	
Maytag	777.6	-1	1515.5	-2	18.8	-38	33.9	-46	2.4	3.9		7.2	23	0.6	
Pier 1 Imports (10)	202.4	46	377.4	37	11.6	50	9.6	-29	5.8	5.6		6.3	27	0.2	
Toro (5)	209.7	-14	397.4	-9	8.5	-3	16.6	6	4.1	3.6		5.8	22	0.7	
Whirlpool	1773.0	4	3389.0	1	58.0	57	82.0	24	3.3	2.2		6.0	26	1.2	
Zenith Electronics	275.0	-18	578.7	-16	-26.9	NM	-50.6	NM	NM	NM		-27.5	NM	-3.1	
(c) BEVERAGES															
GROUP COMPOSITE	12517.5	7	23339.9	8	1167.0	9	1947.7	11	9.3	9.2		23.4	22	1.9	
Anheuser-Busch	2845.3	2	5386.7	4	286.7	11	487.6	11	10.1	9.3		23.1	16	3.1	
Brown-Forman (8)	249.2	11	550.9	15	27.1	10	65.1	17	10.9	11.0		22.3	15	5.2	
Coca-Cola	3039.5	11	5520.5	13	482.4	18	803.3	16	15.9	15.0		38.9	26	2.2	
Coca-Cola Bottling Consolidated	125.1	2	226.9	4	2.7	-9	1.1	12	2.2	2.4		0.2	NM	-0.0	
Coca-Cola Enterprises	1118.6	-1	2023.4	0	33.8	-39	44.5	-30	3.0	4.9		4.3	29	0.5	
Coors (Adolph)	460.0	0	834.7	-2	16.1	-36	22.4	-32	3.5	5.5		2.6	26	0.7	
PepsiCo	4679.8	11	8796.8	12	318.3	9	523.7	10	6.8	7.0		22.6	21	1.4	
(d) PERSONAL CARE															
GROUP COMPOSITE	5246.8	5	10300.0	7	393.2	12	728.3	12	7.5	7.0		33.5	18	2.3	
Alberto-Culver (3)	221.0	10	435.5	10	4.2	-56	13.3	-22	1.9	4.8		13.9	20	1.1	
Avon Products	828.9	4	1598.5	7	52.1	10	70.4	12	6.3	6.0		106.5	16	2.8	
Block Drug (9)	137.3	15	268.7	15	14.3	13	28.3	15	10.4	10.6		13.7	17	3.0	
Church & Dwight	117.9	13	227.3	12	5.7	10	12.2	11	4.8	4.9		23.6	23	1.2	
Colgate-Palmolive	1516.4	4	2978.2	8	93.3	14	184.6	13	6.2	5.6		35.2	16	2.4	
Ecolab	333.1	-11	576.3	-10	15.7	2	11.5	-12	4.7	4.1		13.4	15	1.8	
Gillette	1088.8	6	2203.5	6	101.8	24	209.0	24	9.4	8.0		142.5	21	1.8	
Helene Curtis Industries (10)	223.8	22	473.7	25	2.3	NM	4.8	17	1.0	NM		7.0	27	1.1	
International Flavors & Fragrances	266.1	5	535.8	8	48.8	6	95.9	10	18.4	18.1		18.9	18	4.3	
NCH (8)	163.7	2	339.2	5	9.6	7	20.7	5	5.8	5.6		17.4	13	5.1	
Stanhome	171.3	5	328.2	4	9.5	-22	16.4	-26	5.6	7.4		21.6	15	2.2	
Tambrands	178.4	5	335.1	2	36.0	13	61.4	14	20.2	18.8		43.0	20	2.5	
(e) TOBACCO															
GROUP COMPOSITE	21487.0	12	43036.2	16	1413.6	42	2577.3	48	6.6	5.2		22.9	18	2.4	
American Brands	2937.0*	-1	6794.2	10	181.6	15	398.3	13	6.2	5.4		16.8	13	3.1	
Philip Morris	14770.0*	16	28992.0	20	1153.0	22	2095.0	22	7.8	7.4		32.4	16	4.2	
RJR Nabisco Holdings	3780.0	9	7250.0	9	79.0	NM	84.0	NM	2.1	NM		-6.6	NM	-0.3	
7 CONTAINERS & PACKAGING															
INDUSTRY COMPOSITE	5120.9	13	9771.9	10	170.8	-31	311.9	-34	3.3	5.4		9.6	19	1.8	
(a) GLASS, METAL & PLASTIC															
GROUP COMPOSITE	1829.2	55	3235.0	47	66.3	21	103.4	14	3.6	4.6		12.3	19	3.0	
Ball	638.2	67	1085.6	54	23.0	23	33.7	15	3.6	4.9		13.6	16	2.1	
Constar International	140.6	12	267.4	7	4.5	16	8.2	0	3.2	3.1		9.6	15	1.8	
Crown Cork & Seal	1050.4**	56	1882.0	52	38.7	21	61.5	15	3.7	4.8		12.2	21	3.9	
(b) PAPER															
GROUP COMPOSITE	3291.7	-2	6536.8	-2	104.5	-45	208.5	-45	3.2	5.7		8.9	18	1.5	
Bemis	286.9	2	566.2	2	13.2	-5	21.3	-8	4.6	4.9		16.5	19	1.9	
Federal Paper Board	346.2	9	678.0	7	24.6	-29	52.5	-28	7.1	10.9		10.1	13	2.2	
Longview Fibre (2)	158.1	-3	310.5	-6	3.3	-79	4.7	-83	2.1	9.5		9.9	18	0.7	
Nashua	132.8	-13	263.0	-9	0.7	-86	0.9	-90	0.5	3.3		9.9	15	2.0	
Sonoco Products	422.2	0	829.9	1	22.4	-19	45.2	-14	5.3	6.6		8.2	33	1.0	
Stone Container	1327.2	-7	2664.0	-8	-0.2	NM	1.1	-98	NM	2.1		2.2	41	0.5	
Temple-Inland	618.3	5	1225.2	4	40.6	-38	82.7	-35	6.6	11.2		12.7	14	3.4	

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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS			RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE EARNINGS RATIO 7/26	12 MONTHS' EARNINGS PER SHARE
	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 %	2ND QUARTER 1990 %				
DISCOUNT & FASHION RETAILING														
INDUSTRY COMPOSITE	67154.9	9	147512.3	7	1103.6	27	3606.5	11	1.6	1.4	11.6	26	1.35	
Walmart Department Stores (11)	640.2	-32	1586.0	-32	-47.8	NM	-74.6	NM	NM	NM	NM	NM	-11.28	
Kmart Taylor Stores (11)	111.1**	12	219.3	6	2.0	276	1.3	NM	1.8	0.5	3.2	NM	0.14	
Target To-Go (4)	185.0	19	338.7	17	9.6	83	15.4	114	5.2	3.4	18.9	35	1.10	
Wal-Mart Products (11)	251.7	-38	851.2	-33	-33.4	NM	NA	NA	NM	NM	NM	NA	NA	
Wal-Mart Supercenters (11)	138.1	9	251.8	3	10.4	6	16.4	-15	7.5	7.7	25.9	11	3.82	
Wal-Mart Supercenters (11)	377.4	7	983.5	NA	-21.1	NM	3.9	NA	NM	NM	-1.2	NM	-0.13	
Wal-Mart Supercenters (11)	430.1**	-27	1182.4	-25	-32.4	NM	-97.3	NM	NM	NM	NM	NM	-4.04	
Wal-Mart Supercenters (11)	222.9	16	480.0	10	10.3	48	24.9	41	4.6	3.6	14.2	26	0.85	
Wal-Mart Supercenters (11)	157.8	13	371.3	7	-0.8	NM	6.2	NM	NM	NM	5.0	50	0.16	
Wal-Mart Supercenters (11)	1192.2	26	2440.6	27	16.8	210	38.6	89	1.4	0.6	11.5	44	1.00	
Wal-Mart Supercenters (11)	3349.0**	11	8214.0	10	34.0	-41	269.0	-13	1.0	1.9	17.6	13	5.07	
Wal-Mart Supercenters (11)	921.5**	20	2172.5	15	38.1	30	130.4	14	4.1	3.8	13.6	24	5.20	
Wal-Mart Supercenters (11)	148.3	11	350.1	7	1.2	201	10.1	31	0.8	0.3	11.7	25	0.76	
Wal-Mart Supercenters (11)	299.8	21	721.8	17	8.9	19	38.3	0	3.0	3.0	17.4	14	2.82	
Wal-Mart Supercenters (11)	250.1	15	507.3	14	12.2	57	24.2	42	4.9	3.6	17.0	19	1.36	
Wal-Mart Supercenters (11)	307.2	17	621.0	28	9.7	9	18.1	11	3.1	3.4	14.8	13	2.03	
Wal-Mart Supercenters (11)	490.3	22	1115.0	18	40.9	93	97.4	76	8.3	5.3	33.2	29	1.16	
Wal-Mart Supercenters (11)	248.1	2	396.4	-1	6.2	48	2.2	NM	2.5	1.7	0.5	NM	-0.03	
Wal-Mart Supercenters (11)	391.4	14	700.2	7	7.2	-15	6.3	-63	1.8	2.4	5.2	18	0.63	
Wal-Mart Supercenters (11)	324.9	-28	997.3	-15	-21.3	NM	-260.9	NM	NM	NM	NM	NM	-14.68	
Wal-Mart Supercenters (11)	1186.9	35	2194.4	38	51.3	33	92.8	36	4.3	4.4	14.5	49	0.96	
Wal-Mart Supercenters (11)	262.7	7	530.4	4	4.0	-1	-20.6	NM	1.5	1.6	-4.6	NM	-0.08	
Wal-Mart Supercenters (11)	173.9	-7	449.3	-5	-3.5	NM	-19.5	NM	NM	NM	-21.6	NM	-1.72	
Wal-Mart Supercenters (11)	7706.0**	8	17610.0	4	107.0	7	509.0	536	1.4	1.4	14.1	12	3.81	
Wal-Mart Supercenters (11)	126.5	13	355.8	14	1.5	-12	16.5	-10	1.2	1.5	12.5	27	0.76	
Wal-Mart Supercenters (11)	1284.5**	16	3028.2	13	50.9	-18	223.0	4	4.0	5.6	24.4	27	1.07	
Wal-Mart Supercenters (11)	693.4	-4	1279.4	-3	11.5	-48	16.5	-48	1.7	3.1	8.8	21	1.63	
Wal-Mart Supercenters (11)	1385.6**	-7	3581.8	-9	-116.4	NM	-123.7	NM	NM	NM	NM	NA	-183.75	
Wal-Mart Supercenters (11)	2313.0**	5	5597.0	3	76.0	5	328.0	-10	3.3	3.6	19.1	14	3.86	
Wal-Mart Supercenters (11)	2268.9	16	4315.4	21	59.8	-24	57.4	-33	2.6	4.0	23.3	14	3.31	
Wal-Mart Supercenters (11)	521.7**	6	1308.5	3	24.4	-14	69.1	-15	4.7	5.7	10.1	12	3.25	
Wal-Mart Supercenters (11)	157.2	30	378.0	24	8.7	31	22.7	29	5.5	5.5	21.6	24	0.77	
Wal-Mart Supercenters (11)	766.8	9	1435.6	4	8.0	31	23.6	NM	1.0	0.9	12.1	15	1.44	
Wal-Mart Supercenters (11)	392.3**	6	931.7	2	-7.3	NM	7.1	-68	NM	1.1	NM	NM	-0.41	
Wal-Mart Supercenters (11)	610.6	10	1512.8	7	25.7	95	72.0	61	4.2	2.4	15.2	28	1.57	
Wal-Mart Supercenters (11)	140.8	1	336.3	6	-2.0	NM	-1.0	NM	NM	NM	11.7	16	0.17	
Wal-Mart Supercenters (11)	3715.0	-2	9243.0	-1	80.0	-48	286.0	-45	2.2	4.1	12.7	12	3.99	
Wal-Mart Supercenters (11)	235.1	10	447.6	4	7.2	-23	13.9	-22	3.1	4.4	10.1	25	0.63	
Wal-Mart Supercenters (11)	318.3	6	694.8	1	9.5	28	8.3	-69	3.0	2.5	0.8	NM	0.10	
Wal-Mart Supercenters (11)	110.0	-8	302.0	2	4.8	-20	23.0	12	4.3	5.0	8.4	29	0.56	
Wal-Mart Supercenters (11)	1539.4**	28	2936.2	26	25.1	8	53.0	8	1.6	1.9	18.4	20	2.64	
Wal-Mart Supercenters (11)	192.2	19	442.2	0	1.4	NM	10.4	NM	0.7	NM	-4.5	NM	-0.59	
Wal-Mart Supercenters (11)	313.6	-11	777.4	-8	-0.5	NM	-28.2	NM	NM	0.6	-18.4	NM	-1.63	
Wal-Mart Supercenters (11)	198.6	17	450.3	13	2.0	29	11.9	-29	1.0	0.9	13.6	19	0.74	
Wal-Mart Supercenters (11)	14090.0**	2	26973.8	2	239.3	1	442.0	32	1.7	1.7	7.7	14	2.92	
Wal-Mart Supercenters (11)	747.8	0	1355.5	-1	5.4	349	-7.9	NM	0.7	0.2	519.1	12	1.02	
Wal-Mart Supercenters (11)	416.3	3	864.0	9	1.4	-82	2.4	-84	0.3	1.9	10.9	19	0.94	
Wal-Mart Supercenters (11)	207.1**	-1	531.8	-5	0.2	-93	14.0	-51	0.1	1.5	5.9	18	1.52	
Wal-Mart Supercenters (11)	603.3	17	1317.4	16	14.8	2	30.1	5	2.5	2.8	26.8	18	1.06	
Wal-Mart Supercenters (11)	1025.7	9	3574.2	9	22.4	-33	259.9	-5	2.2	3.5	15.3	28	1.08	
Wal-Mart Supercenters (11)	675.5	1	1381.0	-3	12.3	-29	-43.9	NM	1.8	2.6	-6.5	NM	-0.73	
Wal-Mart Supercenters (11)	314.8**	9	794.3	4	3.7	81	30.1	9	1.2	0.7	39.1	NA	NA	
Wal-Mart Supercenters (11)	616.9	13	1251.3	13	4.4	211	7.8	-10	0.7	0.3	7.4	28	0.75	
Wal-Mart Supercenters (11)	9280.6	37	19639.5	32	307.0	21	788.8	16	3.3	3.7	23.2	39	1.18	
Wal-Mart Supercenters (11)	2127.0**	3	5191.0	7	13.0	-66	162.0	-24	0.6	1.8	12.9	13	2.26	

ELECTRICAL & ELECTRONICS

INDUSTRY COMPOSITE	25833.2	4	50483.7	4	1017.6	-23	2058.8	-15	3.9	5.3	8.4	21	1.57	
ELECTRICAL PRODUCTS														
GROUP COMPOSITE	5835.9	0	11151.8	0	222.8	-44	435.3	-30	3.8	6.9	5.6	36	0.93	
General Industries	1602.3**	1	3099.1	3	109.1	9	173.8	9	6.8	6.3	10.9	18	2.92	
General Industries	197.0	8	379.3	6	23.8	6	46.1	6	12.1	12.2	18.4	18	2.96	
General Industries (4)	404.1	-4	790.8	-3	-23.1	NM	-8.3	NM	NM	6.1	6.7	29	0.89	
General Industries (6)	317.9	8	639.9	9	-26.3	NM	-27.9	NM	NM	NM	-3.6	NM	-0.63	
General Industries & Betts	140.6	-7	291.7	-4	12.3	-18	26.6	-13	8.7	9.9	12.5	21	2.61	
General Industries Electric	3174.0	0	5951.0	-1	127.0	-50	225.0	-51	4.0	7.9	0.8	NM	0.09	
ELECTRONICS														
GROUP COMPOSITE	10929.3	5	21518.3	5	492.2	-12	950.5	-14	4.5	5.4	10.8	13	2.87	
Systems	473.2	8	949.4	6	26.7	18	51.6	16	5.6	5.2	15.2	13	3.18	
General Industries Electronics	2879.4	-3	5600.3	-4	114.3	-40	211.1	-43	4.0	6.4	7.0	13	1.41	
General Industries (5)	1365.5	8	2619.0	4	42.0	-7	82.3	-8	3.1	3.6	12.6	10	7.44	
General Industries (9)	677.0	113	1459.2	91	22.4	26	53.1	24	3.3	5.6	14.1	12	3.67	

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS								RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE- EARNINGS RATIO 7-26	1 MON. EARN. PER SHA
	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	MARGINS						
									2ND QUARTER 1991 %	2ND QUARTER 1990 %					
Motorola	2814.0	4	5557.0	6	119.0	-26	235.0	-18	4.2	5.9	10.3	19	3.3		
Raytheon	2357.0	0	4610.3	1	151.8	5	285.5	4	6.4	6.2	19.1	10	8.6		
Varian Associates (3)	363.2	5	723.1	12	16.0	NM	32.0	NM	4.4	NM	14.2	13	3.0		
(c) INSTRUMENTS															
GROUP COMPOSITE	4162.0	-1	8266.5	-1	122.2	30	267.2	30	2.9	2.2	12.2	17	1.8		
Ametek	182.1	16	361.3	11	9.5	-9	18.1	-11	5.2	6.6	17.8	16	0.8		
Beckman Instruments	220.2	9	416.1	7	9.3	8	17.4	5	4.2	4.2	11.5	14	1.2		
Honeywell	1520.2	-2	2989.2	-3	77.6	-16	149.4	-15	5.1	6.0	20.0	13	4.7		
Imo Industries	253.8	1	515.0	2	2.5	-45	6.3	-50	1.0	1.8	4.5	14	0.8		
Johnson Controls (3)	1137.8	-3	2211.3	-2	29.2	8	39.3	12	2.6	2.3	9.8	16	2.1		
Millipore	185.0	6	372.4	10	15.5	12	30.8	14	8.4	8.0	7.3	32	1.1		
Perkin-Elmer (5)	211.1	1	434.1	2	-39.8	NM	-25.1	NM	NM	4.6	-0.6	NM	-0.0		
Tektronix (7)	321.3	-11	719.1	-8	14.1	NM	27.3	NM	4.4	NM	11.2	18	1.6		
Teradyne	130.5	20	248.1	12	4.3	NM	3.8	NM	3.3	NM	-2.1	NM	-0.2		
(d) SEMICONDUCTORS															
GROUP COMPOSITE	4905.9	12	9547.1	11	180.5	-31	405.8	-19	3.7	5.9	4.7	43	0.6		
Advanced Micro Devices	296.8	11	571.1	6	17.3	NM	21.5	199	5.8	NM	-7.8	NM	-0.6		
AMP	775.7	3	1568.0	3	64.7	-5	134.7	-9	8.3	9.1	15.2	20	2.5		
Analog Devices (2)	142.1	22	275.2	22	6.6	39	10.3	86	4.6	4.0	-2.3	NM	-0.1		
Intel	1252.7	29	2385.5	28	230.8	35	428.2	36	18.4	17.6	18.6	12	3.6		
LSI Logic	181.0	13	361.2	21	4.5	-28	6.6	-10	2.5	3.9	-12.3	NM	-0.8		
Micron Technology (4)	126.8	51	221.3	37	7.0	288	4.8	162	5.5	2.2	0.3	NM	-0.0		
National Semiconductor (7)	444.9	-3	831.7	-3	6.7	123	11.7	NM	1.5	0.7	-24.7	NM	-1.5		
Texas Instruments	1686.0	6	3333.0	7	-157.0	NM	-212.0	NM	NM	0.7	-17.4	NM	-3.7		
10 FOOD															
INDUSTRY COMPOSITE	67113.1	6	131804.2	6	1751.3	10	3392.3	16	2.6	2.5	22.8	20	1.9		
(a) FOOD DISTRIBUTION															
GROUP COMPOSITE	9677.4	6	19196.8	6	98.2	14	197.6	12	1.0	0.9	14.7	13	2.1		
Fleming	3009.7	12	6865.1	10	25.4	25	58.1	19	0.8	0.8	13.0	12	3.2		
Nash Finch	551.1**	-2	1067.3	-1	4.5	0	6.6	4	0.8	0.8	10.8	11	1.6		
Richfood Holdings (8)	304.5	1	543.6	1	3.5	69	5.5	75	1.2	0.7	19.0	16	0.9		
Ryko-Sexton (8)	365.3	1	720.0	2	3.5	69	5.8	112	1.0	0.6	7.5	19	1.1		
Super Food Services (4)	412.6**	1	820.7	1	2.6	-24	4.4	-38	0.6	0.8	11.2	11	1.3		
Super Valu Stores (10)	3604.0	5	6344.8	4	44.9	9	92.1	9	1.2	1.2	16.2	14	2.1		
Wetterau (9)	1430.2	3	2835.3	4	13.7	10	25.2	10	1.0	0.9	23.9	12	2.2		
(b) FOOD PROCESSING															
GROUP COMPOSITE	27778.9	9	53946.9	10	1320.5	6	2466.3	13	4.8	4.9	21.7	20	2.3		
American Maize-Products	141.5	9	258.5	6	4.4	-5	4.5	-43	3.1	3.6	8.5	10	1.9		
Borden	1803.0	-5	3523.8	-7	89.6	-1	153.0	0	5.0	4.8	19.6	14	2.4		
Campbell Soup (5)	1490.8	-2	3261.6	1	76.4	40	211.7	32	5.1	3.6	4.5	NM	0.6		
Castle & Cooke	919.0	16	1617.9	12	53.1	37	78.8	38	5.8	4.9	15.0	18	2.4		
ConAgra (7)	5310.1	32	10184.3	33	98.8	34	164.4	40	1.9	1.8	16.7	20	2.1		
CPC International	1639.6	13	3156.5	13	103.8	9	187.1	8	6.3	6.5	28.9	17	5.0		
Dean Foods (7)	564.2	2	1085.2	1	23.3	10	39.9	16	4.1	3.8	18.6	18	2.6		
General Mills (7)	1829.3	7	3576.9	8	90.9	21	222.2	27	5.0	4.4	41.7	21	2.8		
Gerber Products (9)	281.6	-5	595.0	-2	33.7	8	56.3	3	12.0	10.6	29.2	20	3.0		
Heinz (H. J.) (8)	1838.3	9	3443.3	11	156.1	15	285.0	13	8.5	8.0	30.1	17	2.1		
Hershey Foods	585.2	9	1269.7	4	31.9	-52	80.5	-29	5.5	12.3	14.4	21	2.0		
Hormel (Geo. A.) (2)	697.0	10	1398.2	12	16.6	20	37.0	31	2.4	2.2	16.0	18	1.1		
Hudson Foods (3)	200.1	9	371.8	13	3.1	-30	3.6	-45	1.5	2.4	5.2	21	0.4		
IBP	2665.3	2	5202.4	5	-10.8	NM	-19.8	NM	NM	0.6	1.7	NM	0.1		
Imperial Holly (9)	174.1	-3	332.9	-1	4.6	-16	9.4	26	2.6	3.0	15.4	8	2.0		
International Multifoods (10)	553.4	1	1095.2	2	6.3	21	14.7	58	1.1	1.0	11.2	10	2.7		
Kellogg	1413.7	12	2835.0	15	152.3	12	315.4	36	10.8	10.8	30.4	21	4.8		
McCormick (1)	332.6	10	656.1	9	14.9	-7	30.1	16	4.5	5.3	19.8	23	1.7		
Michael Foods	111.1	-7	224.8	-3	5.1	8	10.9	15	4.6	4.0	17.2	17	1.1		
Pet	430.7	-4	903.6	-1	20.0	42	40.8	17	4.6	3.1	NA	NA	NA		
Pilgrim's Pride (3)	193.3	3	394.5	8	3.0	-58	8.2	-31	1.5	3.7	12.0	12	0.5		
Pioneer Hi-Bred International (4)	729.1	9	867.4	8	161.1	11	150.4	21	22.1	21.6	16.4	16	3.0		
Ralston Purina (3)	1763.3	3	3586.9	5	70.7	-23	169.1	-8	4.0	5.4	49.1	15	3.2		
Seaboard	205.7	57	381.8	49	3.3	-67	9.2	-43	1.6	7.5	10.2	9	15.4		
Smithfield Foods (8)	261.5	16	570.0	22	8.6	202	21.4	186	3.3	1.3	45.9	10	1.9		
Smucker (J. M.) (8)	117.1	8	219.1	7	8.4	8	14.7	6	7.2	7.2	16.7	23	2.1		
Tyson Foods (3)	1016.9	4	1949.2	2	40.6	21	73.6	23	4.0	3.4	19.3	19	1.0		
Universal Foods (3)	210.3	6	401.2	-4	12.4	3	24.3	10	5.9	6.1	20.3	19	2.0		
Wrigley (Wm.) Jr.	301.3	2	583.9	1	38.3	5	70.0	6	12.7	12.3	29.2	20	3.0		
(c) FOOD RETAILING															
GROUP COMPOSITE	29657.0	4	58660.6	3	332.6	26	728.4	30	1.1	0.9	33.2	19	1.33		
Albertson's (11)	2160.2	7	4273.5	8	58.7	15	132.6	19	2.7	2.5	22.2	22	1.8		
American Stores (11)	5411.6	0	11119.8	-4	36.0	29	122.0	51	0.7	0.5	13.8	15	2.7		
Casey's General Stores (8)	136.7**	15	281.6	18	1.0	69	3.5	38	0.7	0.5	10.7	12	0.8		
Dairy Mart Convenience Stores (11)	137.1*	2	278.7	4	-0.3	NM	-0.1	NM	NM	0.2	9.4	12	0.6		

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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS				RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE: EARNINGS RATIO 7-26	12 MONTH EARNINGS PER SHARE
	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 %	2ND QUARTER 1990 %					
Eagle Food Centers (11)	280.1	-1	567.0	-4	2.3	-17	-5.0	NM	0.8	1.0	-4.2	NM	-0.20		
Food Lion	1496.4	17	2913.6	18	49.6	21	93.5	20	3.3	3.2	25.5	30	0.59		
Foodarama Supermarkets (2)	165.7	1	335.3	2	0.4	-35	0.1	-89	0.2	0.4	0.1	NM	-0.03		
Giant Food (16)	783.9	2	1842.6	1	29.3	3	69.0	3	3.7	3.7	20.2	14	2.02		
Great Atlantic & Pacific Tea (10)	3590.7	6	6363.7	7	36.2	-29	67.8	-21	1.0	1.5	11.1	12	3.51		
Hannaford Brothers	492.3**	18	978.2	20	12.0	-1	20.0	-9	2.4	2.9	15.2	22	2.02		
Kroger	5086.4	7	9993.5	7	32.2	28	43.0	187	0.6	0.5	NM	15	1.27		
Penn Traffic (11)	674.1**	-4	1376.3	-8	-4.7	NM	-4.6	NM	NM	NM	NM	NM	-3.42		
Ruddick (3)	377.8	6	740.2	4	7.5	18	13.9	12	2.0	1.8	13.1	11	1.25		
Safeway	3519.8	2	6920.2	2	35.6	51	62.3	61	1.0	0.7	NM	18	1.06		
Seaway Food Town (4)	141.7	4	285.4	3	0.0	-97	0.1	-95	0.0	0.8	4.0	23	0.60		
Smith's Food & Drug Centers	547.0	9	1079.9	9	10.8	27	21.3	27	2.0	1.7	14.1	25	1.54		
Stop & Shop (11)	1447.2	4	2846.6	6	-0.8	NM	23.6	714	NM	NM	16.5	NA	0.72		
Supermarkets General Holding (11)	1469.3	-4	3002.9	-6	-8.8	NM	-4.1	NM	NM	NM	NM	NA	NA		
Village Super Market (5)	169.1	0	343.1	0	0.5	-37	0.9	-64	0.3	0.4	4.2	12	0.71		
Vons	1250.8	2	2474.1	2	15.8	52	28.5	53	1.3	0.9	20.3	19	1.52		
Weis Markets	319.0	0	644.5	2	19.4	-8	40.2	0	6.1	6.7	14.0	16	1.94		
11 FUEL															
INDUSTRY COMPOSITE	104285.8	5	218269.6	7	3746.1	-19	9834.8	11	3.6	4.6	13.3	15	3.00		
(a) COAL															
GROUP COMPOSITE	806.7	1	1582.8	2	15.7	-46	27.1	-15	1.9	3.6	8.8	15	1.58		
Nacco Industries	323.7	-2	628.6	-5	4.7	-53	6.4	-72	1.4	3.0	4.4	29	1.65		
Pittston	483.0**	3	954.2	8	11.0	-43	20.7	125	2.3	4.1	11.7	11	1.56		
(b) OIL & GAS															
GROUP COMPOSITE	97849.9	4	205620.4	7	3433.8	-21	9286.7	11	3.5	4.6	13.4	15	3.21		
Amerada Hess	1433.2**	16	3468.2	20	67.7	NM	143.4	NM	4.7	NM	21.3	7	8.13		
Amoco	6062.0	1	12690.0	2	238.0	-37	730.0	-14	3.9	6.3	12.4	15	3.57		
Ashland Oil (3)	2157.4	2	4051.7	-1	66.7	-33	93.2	-8	3.1	4.7	11.1	12	2.54		
Atlantic Richfield	4238.0*	5	8934.0	8	246.0	-37	597.0	-10	5.8	9.7	22.8	12	9.91		
Burlington Resources	401.5	-2	868.7	-5	33.3	-28	99.0	-15	8.3	11.4	6.5	29	1.37		
Chevron	9700.0**	9	20500.0	12	384.0	-41	941.0	-16	4.0	7.3	13.1	13	5.62		
Coastal	2129.2	14	4666.0	8	26.2	19	80.5	-18	1.2	1.2	10.3	16	1.98		
Crown Central Petroleum	482.2	-2	901.1	-5	8.4	-45	2.4	-85	1.7	3.1	3.9	22	1.24		
Diamond Shamrock	631.3	11	1270.8	10	17.7	45	22.0	33	2.8	2.2	24.4	6	3.35		
Exxon	24536.0**	3	52265.0	8	1125.0	2	3365.0	41	4.6	4.6	18.5	12	4.76		
Fina	823.6	1	1639.5	-5	4.2	-92	12.5	-84	0.5	6.5	5.1	21	3.75		
Holly (5)	112.3	5	235.8	9	3.6	93	6.3	3	3.2	1.7	77.4	11	2.63		
Kerr-McGee	784.2	-5	1569.8	-2	10.3	-66	40.0	-30	1.3	3.7	6.4	21	1.95		
Louisiana Land & Exploration	216.6**	4	403.4	-7	4.5	-30	12.8	-35	2.1	3.1	10.6	21	1.69		
Mapco	649.4**	7	1351.6	9	3.0	-93	58.9	-25	0.5	6.8	30.3	13	3.63		
Maxus Energy	186.9	34	397.3	33	-13.6	NM	0.4	NM	NM	NM	NM	NM	-0.20		
Mitchell Energy & Development (11)	198.1	20	444.4	22	9.2	38	26.8	49	4.7	4.0	8.2	17	1.07		
Mobil	14449.0***	5	31029.0	8	445.0	-11	1155.0	29	3.1	3.6	13.2	13	5.28		
Occidental Petroleum	5056.0	-1	10359.0	1	135.0	96	218.0	22	2.7	1.3	-39.9	NM	-5.69		
Oryx Energy	341.0	5	778.0	-3	-15.0	NM	67.0	81	NM	NM	36.0	12	2.65		
Pennzoil	598.6**	9	1147.8	4	13.0	173	34.9	-7	2.2	0.9	7.3	32	2.28		
Phillips Petroleum	3150.0	10	6435.0	8	33.0	-69	219.0	74	1.0	3.7	22.9	11	2.49		
Quaker State	211.7	-5	400.2	-7	5.9	-31	6.1	-43	2.8	3.8	5.0	25	0.55		
Sun	3090.0***	7	6140.0	2	43.0	-63	84.0	-46	1.4	4.0	3.9	24	1.20		
Texaco	9031.0**	4	19211.0	7	269.0	-24	684.0	0	3.0	4.0	16.1	12	5.23		
Tosco	505.7	-12	1001.5	-5	20.4	-58	39.8	-3	4.0	8.3	33.5	4	4.69		
Union Texas Petroleum Holdings	248.3**	6	603.3	6	143.5	820	201.3	330	57.8	5.9	60.1	8	2.42		
Unocal	2453.0**	-2	4911.0	-1	5.0	-97	80.0	-67	0.2	6.6	9.2	24	1.02		
Unocal Exploration	197.7**	14	471.5	25	12.6	-55	85.4	-13	6.4	16.4	19.1	18	0.60		
USX-Marathon Group	3503.0	14	6916.0	9	64.0	-50	135.0	-36	1.8	4.2	11.9	15	1.67		
Valero Energy	273.1	-1	560.0	4	25.3	27	45.9	55	9.3	7.2	15.5	9	2.63		
(c) PETROLEUM SERVICES															
GROUP COMPOSITE	5629.3	11	11066.4	14	296.6	6	521.0	4	5.3	5.5	12.1	24	1.56		
Baker Hughes (3)	708.9	0	1414.7	8	45.1	19	85.5	25	6.4	5.3	11.5	20	1.23		
Baroid	186.2	30	340.6	28	6.8	22	10.4	62	3.7	3.9	9.1	21	0.32		
Dresser Industries (2)	1161.0	10	2260.4	17	24.8	-38	38.9	-35	2.1	3.8	9.0	19	1.14		
Grace Energy	124.5**	10	258.0	14	3.2	53	7.3	-9	2.6	1.9	3.7	17	0.88		
Halliburton	1787.7**	6	3520.1	7	32.3	-31	59.7	-28	1.8	2.8	7.8	23	1.63		
Schlumberger	1552.7	20	3063.7	22	180.8	25	313.7	15	11.6	11.2	18.7	26	2.57		
Smith International	108.3**	26	208.8	27	3.5	126	5.5	253	3.2	1.8	10.5	37	0.35		
12 HEALTH CARE															
INDUSTRY COMPOSITE	39747.9	12	79196.3	12	4057.1	25	8262.9	34	10.2	9.1	26.4	21	2.66		
(a) DRUG DISTRIBUTION															
GROUP COMPOSITE	9464.9	11	19097.8	10	161.4	12	367.4	10	1.7	1.7	15.1	18	1.53		
Bergen Brunswig (4)	1242.0**	9	2403.7	8	17.1	-4	34.2	3	1.4	1.6	14.1	14	1.91		
Big B (11)	132.7	8	269.0	5	1.9	383	4.4	259	1.4	0.3	0.1	NM	0.01		
Bindley Western Industries	545.9	13	1091.4	19	2.1	19	4.1	21	0.4	0.4	12.5	14	1.08		

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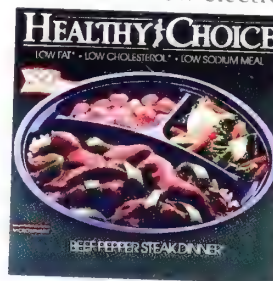
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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS				RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE-EARNINGS RATIO 7-26	12 MONTH EARNINGS PER SHARE
	2ND QUARTER 1991	CHANGE FROM 1990	6 MONTHS 1991	CHANGE FROM 1990	2ND QUARTER 1991	CHANGE FROM 1990	6 MONTHS 1991	CHANGE FROM 1990	2ND QUARTER 1991	2ND QUARTER 1990					
	\$ MIL	%	\$ MIL	%	\$ MIL	%	\$ MIL	%	%	%					
Cardinal Distribution (9)	345.3	43	686.5	43	4.9	47	10.7	42	1.4	1.4		9.8	31	1.3	
Drug Emporium (10)	178.7	27	361.2	30	1.0	-46	2.1	-52	0.6	1.3		9.8	17	0.4	
Durr-Fillauer Medical	233.3	14	455.3	12	5.5	33	9.6	24	2.4	2.0		14.6	18	1.4	
Eckerd (Jack) (11)	898.7	6	1859.6	1	5.1	146	18.4	-23	0.6	0.2		NM	NA	NA	
Fay's (11)	177.2	16	367.8	17	1.8	24	6.9	38	1.0	1.0		16.4	17	0.8	
Genovese Drug Stores (11)	132.9	3	246.0	3	1.4	37	4.1	141	1.1	0.8		14.8	15	0.8	
Longs Drug Stores (11)	569.2	6	1250.1	9	14.1	-5	31.3	-7	2.5	2.8		15.5	14	2.9	
McKesson (9)	2241.7**	11	4415.5	7	27.1	5	54.3	23	1.2	1.3		17.6	14	2.5	
Perry Drug Stores (2)	155.4	-2	326.5	-3	1.1	84	2.6	-29	0.7	0.4		-1.0	NM	-0.0	
Rite Aid (10)	907.4	9	1839.9	9	28.9	15	67.9	13	3.2	3.0		14.3	15	1.3	
Walgreen (4)	1704.4	12	3525.2	11	49.3	13	116.8	11	2.9	2.9		18.0	21	1.5	
(b) DRUGS & RESEARCH GROUP COMPOSITE															
	15276.4	11	30579.9	14	2596.4	26	5401.5	23	17.0	15.0		31.0	22	3.0	
Allergan	225.8	2	437.6	5	18.5	8	34.2	11	8.2	7.7		15.7	15	1.2	
American Home Products	1619.5	1	3383.8	-1	265.2	-2	617.7	6	16.4	16.8		44.0	16	4.0	
Amgen (9)	153.9	115	293.4	128	-48.4	NM	-11.5	NM	NM	15.6		-6.8	NM	-0.7	
Bristol-Myers Squibb	2730.4	10	5465.4	11	489.5	17	982.1	19	17.9	16.8		35.4	23	3.6	
Carter-Wallace (9)	170.7	11	336.7	13	15.7	9	24.1	0	9.2	9.4		13.9	19	3.4	
Genentech	117.6**	9	236.1	12	11.4	114	30.7	65	9.7	4.9		-9.2	NM	-1.0	
Lilly (Eli)	1376.3	12	2811.8	14	317.5	16	706.1	15	23.1	22.4		26.0	17	4.2	
Marion Merrell Dow	718.0	14	1362.0	13	162.0	25	301.0	25	22.6	20.7		41.6	19	1.9	
Merck	2122.4	12	4171.3	14	556.0	18	1039.5	19	26.2	24.8		48.0	25	5.0	
Pfizer	1631.1	9	3326.8	12	179.1	18	446.5	11	11.0	10.1		16.3	24	2.5	
Rhone-Poulenc Rorer	924.8	33	1852.5	90	68.3	NM	122.0	NM	7.4	NM		39.6	19	2.2	
Schering-Plough	912.9	6	1862.2	8	167.4	16	340.6	16	18.3	16.7		30.8	19	2.7	
Syntex (5)	470.7	21	914.8	25	112.1	24	213.6	31	23.8	23.2		42.6	22	1.8	
Upjohn	864.0	15	1670.1	13	127.5	12	260.8	13	14.8	15.2		30.4	16	2.6	
Warner-Lambert	1238.2	7	2455.4	9	154.6	15	294.1	15	12.5	11.6		35.8	17	3.9	
(c) HEALTH CARE SERVICES GROUP COMPOSITE															
	5880.5	17	11366.7	14	312.4	63	572.6	53	5.3	3.8		17.3	18	1.3	
American Medical Holdings (4)	667.4	7	1320.7	8	4.7	697	-4.7	NM	0.7	0.1		-12.8	NM	-0.7	
Beverly Enterprises	563.8	8	1109.7	9	8.2	148	12.6	217	1.5	0.6		5.1	37	0.2	
Community Psychiatric Centers (1)	116.9	16	219.0	19	26.7	12	47.9	12	22.9	23.7		18.5	15	1.9	
Hillhaven (7)	325.4**	10	637.9	11	1.3	272	1.4	75	0.4	0.1		1.0	NM	0.0	
Humana (4)	1593.0	25	2972.0	21	101.0	18	188.0	17	6.3	6.7		18.6	15	2.1	
Lifetime	213.3	28	418.3	28	4.7	17	9.2	21	2.2	2.4		12.7	14	1.9	
Manor Care (7)	218.3	18	416.4	16	9.1	22	14.4	16	4.2	4.0		13.5	23	0.8	
National Health Laboratories	154.1	21	296.0	19	27.0	26	51.5	24	17.5	16.9		33.7	22	0.9	
National Medical Enterprises (7)	1009.8	14	1965.4	3	79.1	14	150.3	14	7.8	7.8		20.3	14	3.4	
PacificCare Health Systems (3)	316.6	26	616.7	24	8.2	69	15.2	74	2.6	1.9		28.6	20	1.9	
Republic Health (4)	119.7	32	229.9	7	1.5	NM	2.7	NM	1.2	NM		11.9	NA	NA	
U. S. Healthcare	413.5**	27	814.2	26	35.1	155	68.6	166	8.5	4.2		45.2	20	1.6	
Universal Health Services	168.7	4	350.4	3	5.8	66	15.5	71	3.5	2.2		10.4	13	1.2	
(d) MEDICAL PRODUCTS GROUP COMPOSITE															
	9126.2	11	18152.0	12	986.8	16	1921.5	81	10.8	10.3		22.8	21	2.7	
Abbott Laboratories	1683.0	12	3336.6	13	268.3	12	522.4	12	15.9	16.0		34.9	22	2.3	
Bard (C. R.)	218.7	13	430.2	11	14.4	43	28.0	45	6.6	5.2		14.2	26	0.9	
Bausch & Lomb	396.8	13	736.2	10	36.7	16	62.4	16	9.2	8.9		17.5	18	2.3	
Baxter International	2197.0	10	4319.0	11	141.0	28	251.0	NM	6.4	5.5		13.9	18	1.9	
Becton, Dickinson (3)	554.6	12	1111.4	9	49.0	5	98.0	6	8.8	9.4		15.4	13	4.8	
Johnson & Johnson	3031.0	8	6180.0	10	406.0	15	824.0	38	13.4	12.6		27.8	21	4.1	
Medtronic (8)	281.3	15	533.6	16	40.2	23	74.4	22	14.3	13.4		20.4	28	4.5	
Mine Safety Appliances	124.9	6	243.3	6	5.0	-36	10.7	-25	4.0	6.7		9.2	12	3.9	
Owens & Minor	321.5	7	634.5	7	2.7	39	5.1	45	0.9	0.7		11.8	21	0.8	
U. S. Surgical	203.2	70	393.3	75	21.2	97	37.4	96	10.5	9.0		25.0	62	1.1	
Westmark International	114.2	-10	233.8	-4	2.2	-51	8.1	-15	1.9	3.6		5.3	27	1.5	
(e) HOUSING & REAL ESTATE															
INDUSTRY COMPOSITE	7488.7	-4	13884.7	-6	203.1	-54	122.9	-82	2.7	5.6		8.7	27	0.8	
(f) BUILDING MATERIALS GROUP COMPOSITE															
	6044.5	-3	11123.7	-6	180.3	-54	97.4	-83	3.0	6.2		9.3	29	0.8	
Ameron (1)	114.2	-2	222.5	8	1.3	-70	0.8	-77	1.2	3.7		6.3	15	2.3	
Barnes Group	140.2	-1	271.1	-4	4.9	5	6.8	-18	3.5	3.3		12.2	14	2.5	
Hughes Supply (11)	116.5	-16	234.8	-13	-1.3	NM	-3.2	NM	NM	1.2		-1.0	NM	-0.2	
Lafarge	428.5	-11	644.8	-13	4.3	-87	-74.8	NM	1.0	6.8		-1.7	NM	-0.0	
Manville	519.1	-2	987.1	-3	4.9	-90	38.2	-45	0.9	9.1		7.7	15	0.4	
Owens-Corning Fiberglas	745.0	-3	1365.0	-10	15.0	-62	-8.0	NM	2.0	5.1		NM	NM	-0.1	
Ply-Gem Industries	159.6	5	270.5	-1	2.8	-22	-0.9	NM	1.7	2.3		0.5	NM	0.0	
PPG Industries	1477.9	-6	2854.6	-6	79.1	-44	101.0	-62	5.4	9.0		12.2	19	2.9	
RPM (1)	132.8	0	235.3	0	7.8	14	11.1	12	5.8	5.1		15.4	21	1.0	
Sherwin-Williams	722.8	18	1250.9	13	47.7	6	55.2	1	6.6	7.3		16.0	18	1.4	
Southdown	137.4**	-9	241.3	-14	-2.2	NM	-9.7	NM	NM	5.3		-4.9	NM	-0.9	
Tecumseh Products	327.7	-10	645.2	-17	14.2	27	19.1	-29	4.3	3.1		0.9	87	1.1	

Footnotes on page 53

A red umbrella with a dark handle leans against a white desk. The desk holds a multi-line office phone, a pen holder with various pens and scissors, and a computer keyboard. In the background, there are stacks of papers and a computer monitor. The umbrella's tip rests on the floor near an office chair.

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**INTRODUCING
THE RE-DESIGNED,
RE-CALIBRATED,
RE-ENGINEERED,
RE-INVENTED
BMW 3-SERIES.**

In today's volatile economy, even people of means are asking a question that should alarm the world's automobile makers:

"Just what makes this car worth the money?"

The new BMW 325i sedan, however, welcomes such scrutiny. Because not only does it embody

the traditional BMW passion for driving, it offers a whole set of more practical-minded virtues—most notably safety, durability and ease of maintenance.

It represents eight years of intensive thought from every automotive discipline. An effort unlike any in BMW's history.

**THE NEXT BEST THING TO A
CAR THAT MAINTAINS ITSELF.**

At the heart of the 325i is a new 189-hp, 24-valve engine so advanced that it requires little regular maintenance beyond the changing of oil, filters and plugs.

Its sophisticated electronics

incorporate a "black box" system that can play back past engine events for the BMW technicians, revealing problems that might otherwise be difficult to detect. Or even describe.

**THE 325i IMPACT-ACTIVATED
SAFETY SYSTEM.**

BMW has always held that the greatest safety feature is a car that enhances the driver's ability to avoid accidents in the first place. Thus, BMW's historical excellence in the areas of suspension, steering and advanced antilock brake technology.

But, in the event that you



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unable to avoid a frontal impact, the 325i is also designed to launch an entire sequence of events to help minimize injuries.

Hydraulic bumpers absorb part of the impact energy. A system of "crush tubes" absorbs more. The seat belts tighten for grip. Three sensors trigger the driver's-side airbag. Interior lights are automatically turned off and the doors are unlocked, to assist in escape or rescue.

A SAFE CAR NEEDN'T BE A BORING ONE.

The unique driving character of the original 3-Series is not

only alive in the new 325i sedan, but substantially enhanced.

The rear suspension is so unlike other cars in its class, it's patented. Resulting in improved stability in hard cornering, and a better grip of the road overall.

When it comes to comfort, the 325i is now longer, taller and wider than before. It has firmly supported seats. Left and right temperature controls, to allow for individual preferences. Even a microfiltration system that removes dust, pollen and most odors from the interior air.

Of course, the 325i is also equipped with BMW's four-year/

50,000-mile bumper-to-bumper warranty,* for protection against unexpected expenses, as well as a Roadside Assistance program you can call upon any day of the year, on any road in the U.S.A.**

If you would like to receive literature on the new 3-Series, or be connected directly to your nearest BMW dealer, you need only call 800-334-4BMW.

We also invite you to stop in for a test drive, so you can find out what makes the 325i sedan worth the money from the best vantage point of all: the driver's seat.

THE ULTIMATE DRIVING MACHINE.®



* Your BMW dealer for details on this limited warranty. ** Services provided by Cross Country Motor Club, Inc., Boston, MA 02155, except in CA, where services are provided by Cross Country Motor Club of Calif., Inc., Boston, MA.

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE-EARNINGS RATIO 7-26	12 MONTH EARNINGS PER SHARE
	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 %	2ND QUARTER 1990 %			
Texas Industries (7)	160.3	-6	303.4	-2	0.2	NM	-4.6	NM	0.1	NM	7.8	11	1.9
USG	434.0	-11	850.0	-13	-31.0	NM	-66.0	NM	NM	NM	NM	NM	-2.2
Valspar (2)	162.1	8	283.8	8	6.7	0	8.8	-11	4.2	4.5	19.2	19	2.3
Vulcan Materials	266.4	-10	463.4	-12	25.9	-35	23.7	-59	9.7	13.4	12.9	16	2.2
(b) CONSTRUCTION & REAL ESTATE GROUP COMPOSITE	1444.2	-5	2761.0	-7	22.8	-50	25.5	-73	1.6	3.0	6.1	19	0.90
Centex (9)	544.8**	-4	1056.7	-6	5.8	-65	10.0	-69	1.1	2.9	6.8	17	2.1
Kaufman & Broad Home (1)	307.2	-12	626.2	-6	3.8	-75	6.4	-78	1.2	4.3	7.6	20	0.5
PHM	296.6**	5	550.8	4	7.9	-7	8.2	-60	2.7	3.0	5.4	19	0.7
Ryland Group	295.5	-9	527.3	-18	5.3	-8	0.9	-93	1.8	1.8	3.8	28	0.6
14 LEISURE TIME INDUSTRIES													
INDUSTRY COMPOSITE	18079.6	4	34609.6	4	926.1	-21	1458.6	-25	5.1	6.7	11.6	22	1.4
(a) EATING PLACES GROUP COMPOSITE	3495.8	2	6798.0	3	244.1	5	398.0	11	7.0	6.8	19.0	16	1.4
Bob Evans Farms (8)	124.8	7	251.2	9	8.4	28	17.2	37	6.8	5.6	13.9	17	1.0
Karcher (Carl) Enterprises (11)	164.5	5	282.7	3	2.7	-49	3.3	NM	1.6	3.4	13.2	16	0.5
McDonald's	1670.8	1	3228.6	2	232.0	8	400.5	7	13.9	13.0	20.2	14	2.2
Morrison (7)	250.4**	6	497.7	7	6.9	115	14.3	77	2.8	1.4	14.7	15	1.6
Shoney's (2)	239.2**	7	514.6	7	10.6	24	16.6	25	4.4	3.8	NM	19	0.8
Sizzler International (8)	121.2	17	263.7	14	2.5	-53	8.4	-29	2.1	5.2	9.0	17	0.8
TW Holdings	924.9	0	1759.5	-1	-19.0	NM	-62.4	NM	NM	NM	-74.4	NM	-0.6
(b) ENTERTAINMENT GROUP COMPOSITE	2888.2	6	5717.0	8	138.5	-50	227.5	-54	4.8	10.0	11.2	25	1.9
Blockbuster Entertainment	210.1	41	386.9	34	21.4	44	37.3	32	10.2	10.0	22.9	21	0.4
Commtron (4)	126.3**	-13	238.2	-9	1.2	-47	3.1	-25	1.0	1.6	11.8	7	0.8
Disney (Walt) (3)	1511.6	-2	2950.6	4	165.5	-31	292.2	-30	10.9	15.5	19.5	23	5.2
Orion Pictures (10)	172.1	87	376.1	64	5.4	NM	-42.7	NM	3.1	NM	-37.1	NM	-2.5
Paramount Communications (2)	868.1	7	1765.2	7	-55.0	NM	-62.3	NM	NM	2.6	4.1	31	1.2
(c) HOTEL & MOTEL GROUP COMPOSITE	3030.1	9	5846.1	8	102.4	2	136.2	-29	3.4	3.6	9.3	44	0.7
Azlar	123.3	-6	234.8	-8	2.5	NM	-2.5	NM	2.0	NM	-1.1	NM	-0.0
Caesars World (5)	220.2	1	428.0	2	13.2	25	17.1	44	6.0	4.8	13.1	16	1.6
Circus Circus Enterprises (11)	197.1	48	373.4	48	26.3	37	41.1	30	13.4	14.4	38.9	50	1.5
Hilton Hotels	287.2**	5	554.1	3	23.6	-38	35.9	-43	8.2	14.0	9.2	24	1.7
Marriott	1940.0	10	3767.0	9	27.0	-41	37.0	-50	1.4	2.6	2.4	NM	0.0
Promus	262.3	3	488.7	0	9.8	15	7.6	-71	3.7	3.4	2.3	NM	0.1
(d) OTHER LEISURE GROUP COMPOSITE	8665.5	2	16248.5	2	441.2	-22	697.0	-23	5.1	6.7	9.5	21	1.4
American Greetings (10)	334.1	9	710.5	10	21.6	12	43.7	14	6.5	6.3	10.6	12	2.6
Brunswick	546.7	-18	1039.7	-23	-9.0	NM	-17.5	NM	NM	2.9	2.4	68	0.2
Carnival Cruise Lines (1)	345.6	-2	673.9	10	43.4	-21	73.9	-7	12.6	15.5	18.6	15	1.4
Eastman Kodak	4989.0	2	9411.0	5	357.0	-7	535.0	-8	7.2	7.9	9.7	20	2.0
Fleetwood Enterprises (8)	383.1	-11	662.2	-15	11.1	-35	13.0	-50	2.9	4.0	7.2	24	1.3
Harley-Davidson	265.3	6	461.5	-1	16.3	1	20.8	-26	6.1	6.4	15.3	22	1.7
Hasbro	368.5	33	675.1	17	-31.1	NM	-10.7	NM	NM	3.1	5.8	33	0.8
Huffy	189.3	28	357.9	29	7.2	2	13.3	1	3.8	4.8	16.2	13	1.4
Mattel	322.5	1	584.7	6	22.1	9	32.2	12	6.8	6.4	29.3	13	1.8
Outboard Marine (3)	285.4	-8	519.8	-16	-23.2	NM	-46.8	NM	NM	NM	-22.1	NM	-5.7
Polaroid	521.4	10	962.6	6	26.8	-19	43.2	-33	5.1	6.9	41.8	15	1.7
Tyco Toys	114.6	11	189.6	9	-0.9	NM	-3.1	NM	NM	2.9	-3.7	NM	-0.5
15 MANUFACTURING													
INDUSTRY COMPOSITE	24010.9	-2	46800.4	-1	899.0	-26	1484.7	-35	3.7	4.9	10.1	21	1.9
(a) GENERAL MANUFACTURING GROUP COMPOSITE	9272.9	2	18349.4	4	583.9	-11	1105.5	-12	6.3	7.3	16.5	19	2.7
Alliant Techsystems	260.7	-21	556.2	-2	10.2	12	14.9	8	3.9	2.7	18.6	NA	NA
Avery Dennison	626.6	-5	1286.5	1	15.6	-30	32.7	-30	2.5	3.4	NA	NM	-0.1
Blount (10)	136.7	-20	280.5	-14	-3.0	NM	-5.0	NM	NM	0.7	-2.1	NM	-0.2
Carlisle	156.4	-3	300.5	-4	3.5	-47	5.8	-46	2.2	4.1	8.6	15	2.2
Corning	778.2	15	1469.4	15	73.9	10	121.1	7	9.5	9.9	15.7	21	3.1
Crane	339.2	-11	645.4	-12	12.8	-20	22.1	-25	3.8	4.2	17.5	16	1.7
Federal Signal	119.4	3	229.9	5	8.6	10	14.3	9	7.2	6.7	20.1	19	1.2
Harsco	454.5	1	909.0	8	12.2	-45	24.1	-31	2.7	4.9	14.0	12	2.3
Hillenbrand Industries (1)	301.0	8	584.4	5	22.5	10	41.9	4	7.5	7.3	16.9	21	2.1
Illinois Tool Works	673.1	3	1281.3	5	47.3	-5	88.5	-2	7.0	7.6	15.7	17	3.2
Keystone International	122.5	8	235.5	9	11.5	1	20.5	-4	9.4	10.1	18.8	24	1.2
Mark IV Industries (10)	286.0	28	549.8	30	7.4	1	12.1	0	2.6	3.3	14.0	7	1.7
Minnesota Mining & Mfg.	3349.0	4	6738.0	5	299.0	-13	599.0	-12	8.9	10.6	19.8	16	5.5
Newell	261.3	0	503.6	-3	25.5	16	45.6	-1	9.7	8.4	19.1	22	1.6
Robertson Ceco	195.7	55	377.1	61	-10.0	NM	-20.7	NM	NM	NM	-15.2	NM	-1.4
Rubbermaid	417.3	10	828.2	9	39.1	12	77.7	11	9.4	9.2	18.7	29	1.8

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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE- EARNINGS RATIO 7-26	12 MONTHS' EARNINGS PER SHARE
	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 %	2ND QUARTER 1990 %			
degar Industries	122.3	-18	236.3	-20	1.7	NM	1.1	NM	1.4	NM	-15.1	NM	-1.94
nova	432.9	-14	867.7	-12	3.8	-79	5.7	-82	0.9	3.6	3.4	39	0.66
Imont Industries	239.9	12	470.0	10	2.4	-55	4.1	-58	1.0	2.5	8.7	16	0.85
CHINE & HAND TOOLS DUP COMPOSITE	2836.4	-7	5606.2	-4	46.9	-62	69.6	-70	1.7	4.0	5.7	29	0.87
ck & Decker	1106.5	-10	2194.1	-2	7.3	-55	11.4	-56	0.7	1.3	4.2	26	0.59
cinnati Milacron	173.1	-10	354.1	-6	-4.5	NM	-10.4	NM	NM	1.6	-15.9	NM	-1.48
rk Equipment	306.4	-11	612.8	-16	-11.6	NM	-27.4	NM	NM	4.4	-1.7	NM	-0.52
aher	201.9**	-1	405.6	6	4.2	-63	8.2	-63	2.1	5.7	7.0	29	0.75
nnametal (6)	155.7	0	313.5	-1	1.9	-79	7.9	-60	1.2	5.7	8.7	19	2.00
ap-on Tools	225.3**	-6	448.3	-7	19.8	-27	37.2	-36	8.8	11.3	12.0	17	1.93
K	177.5	-12	334.2	-9	3.6	-64	1.1	-92	2.0	4.9	2.3	43	0.34
nley Works	490.0	-2	943.6	-4	26.2	-14	41.7	-21	5.3	6.1	14.0	18	2.33
SPECIAL MACHINERY DUP COMPOSITE	9453.2	-4	18091.4	-5	257.1	-37	340.8	-57	2.7	4.1	7.1	22	1.80
plied Materials (2)	166.1	16	310.7	10	7.3	-30	11.5	-47	4.4	7.3	7.9	21	1.41
IP Holding	115.5	23	220.0	18	6.5	-19	17.3	0	5.7	8.5	46.5	21	0.86
terpillar	2691.0	-9	5366.0	-9	-17.0	NM	-49.0	NM	NM	1.6	0.4	NM	0.17
ere (2)	1925.3**	-9	3363.0	-11	73.1	-49	30.0	-87	3.8	6.8	7.4	18	2.87
ver	557.0	-1	1110.4	2	35.1	-17	64.5	-18	6.3	7.5	17.8	16	2.35
C	1046.6	6	1924.0	7	62.5	14	101.2	9	6.0	5.5	97.8	11	4.53
neral Signal	410.9	-7	808.4	-7	15.2	NM	29.4	672	3.7	NM	2.7	71	0.64
ulds Pumps	147.4	4	279.3	4	9.2	5	16.0	6	6.3	6.2	14.9	15	1.52
rnischfeger Industries (2)	418.0	-5	797.1	-8	17.8	1	31.5	-2	4.3	4.0	11.9	10	2.18
erroll-Rand	922.6	-1	1786.8	-3	32.8	-39	61.2	-38	3.6	5.8	9.6	18	2.84
erlake	178.5	-13	357.7	-11	-2.8	NM	-7.8	NM	NM	NM	NM	NM	-1.80
stair	283.8	-4	572.9	-1	8.9	26	16.3	28	3.1	2.4	14.0	11	2.86
wart & Stevenson Services (11)	154.0	7	322.5	-3	7.8	8	14.3	-8	5.1	5.0	15.8	22	2.00
iken	436.5	0	872.7	3	0.7	-97	4.5	-90	0.2	5.8	1.5	52	0.52
TILES DUP COMPOSITE	2448.3	-4	4753.3	-4	11.1	-47	-31.3	NM	0.5	0.8	-2.3	NM	0.15
any International	142.7**	7	276.3	4	4.4	20	4.4	-29	3.1	2.8	2.6	80	0.23
/G (8)	297.6	-4	617.7	-2	-9.8	NM	-14.9	NM	NM	NM	-17.5	NM	-0.68
ldcrest Cannon	306.8	-3	567.3	-4	1.6	NM	-1.9	NM	0.5	NM	-14.4	NM	-3.27
erface	145.0	-4	296.4	-3	2.1	-66	3.8	-69	1.5	4.1	8.4	14	0.88
aw Industries (6)	429.9	1	771.4	-6	10.0	-54	10.3	-72	2.3	5.1	16.6	31	1.15
ings Industries	482.7	-1	913.1	-3	5.7	-46	7.2	-61	1.2	2.2	-3.2	NM	-1.03
ifi (6)	122.3	14	234.5	14	11.4	28	21.1	37	9.3	8.3	28.7	19	2.02
ckes (11)	521.3	-14	1076.5	-10	-14.3	NM	-61.3	NM	NM	NM	-8.8	NA	NA
ETALS & MINING													
USTRY COMPOSITE	14174.3	-9	27705.6	-9	252.9	-71	240.4	-86	1.8	5.7	1.7	44	0.74
MINIMUM DUP COMPOSITE	5628.0	-3	10892.8	-4	165.1	-56	346.3	-49	2.9	6.5	5.9	19	2.61
imum Co. of America	2569.3	-5	4979.3	-7	81.2	-50	178.2	-43	3.2	6.0	3.3	37	1.94
iax	968.8	-2	1897.2	-1	5.0	-91	37.0	-65	0.5	5.8	6.9	13	1.78
ixxam	577.5	-5	1141.0	-4	17.5	-70	42.2	-50	3.0	9.4	24.3	4	11.00
ynolds Metals	1512.4	-1	2875.3	-2	61.4	-40	88.9	-51	4.1	6.7	7.0	18	3.45
EL DUP COMPOSITE	6445.6	-13	12616.9	-12	-70.6	NM	-459.1	NM	NM	3.0	-13.2	NM	-1.71
egheny Ludlum	264.8	-11	531.3	-8	10.8	-52	23.3	-49	4.1	7.6	12.8	19	1.41
nco	388.7	-15	799.2	-12	-28.5	NM	-68.1	NM	NM	NM	-11.1	NM	-1.01
hlehem Steel	1115.0	-13	2170.6	-13	-29.1	NM	-68.3	NM	NM	1.7	-53.0	NM	-7.92
pernter Technology (6)	149.9	-3	296.6	-5	7.6	-38	14.0	-47	5.1	7.9	9.5	14	3.52
mmercial Metals (4)	288.0**	1	567.9	1	2.8	-56	4.3	-63	1.0	2.2	7.5	15	1.39
lops Industries	276.2	-10	531.2	-12	-5.3	NM	-8.9	NM	NM	NM	-6.0	NM	-0.58
rida Steel (3)	118.6	-17	223.3	-19	-2.8	NM	-6.3	NM	NM	2.8	NM	NA	NA
and Steel Industries	864.8	-14	1697.5	-15	-25.0	NM	-65.0	NM	NM	2.0	-11.4	NM	-4.89
ie Star Technologies	129.6	-11	279.7	-4	8.4	-13	17.5	-2	6.5	6.6	29.5	4	2.22
ens	178.0	-1	334.1	-4	13.0	11	21.8	-4	7.3	6.5	19.9	9	4.96
rthwestern Steel & Wire (5)	123.5	7	236.8	11	-7.6	NM	-7.5	NM	NM	2.5	-5.2	NA	-0.27
cor	371.7	-2	722.2	-1	13.4	-28	27.4	-19	3.6	4.9	10.3	23	3.20
egon Steel Mills	136.9	75	255.8	67	12.9	60	24.3	61	9.4	10.3	16.5	17	2.15
anex (2)	142.6	-14	285.1	-8	2.1	-71	4.6	-59	1.5	4.4	13.2	11	1.60
X-U. S. Steel Group	1161.0	-26	2277.0	-24	-39.0	NM	-347.0	NM	NM	5.3	-11.4	NM	-4.28
irton Steel	249.9	-17	503.1	-18	-19.8	NM	-48.3	NM	NM	2.1	-20.7	NM	-2.86
eeeling Pittsburgh	254.1	-12	477.6	-12	2.0	-94	3.5	-94	0.8	12.7	NM	NA	NA
orthington Industries (7)	232.2	-10	427.7	-11	13.5	-29	19.7	-38	5.8	7.4	12.8	24	1.13
OTHER METALS DUP COMPOSITE	2100.7	-12	4195.9	-9	158.4	-43	353.2	-37	7.5	11.7	15.2	13	2.71
arco	458.9	-16	924.1	-13	15.4	-69	23.4	-73	3.4	9.2	5.8	12	2.10
prus Minerals	412.8	-11	831.4	-7	20.0	-25	41.2	-29	4.8	5.8	7.2	11	2.00
igma Copper	162.9	-19	333.3	-12	8.2	-64	15.2	-55	5.0	11.2	10.1	3	1.85

CORPORATE SCOREBOARD

COMPANY	SALES			PROFITS			MARGINS				RETENTION		
	END QUARTER	CHANGE FROM	12 MONTHS	END QUARTER	CHANGE FROM	12 MONTHS	END QUARTER	END QUARTER	END QUARTER	END QUARTER	COMMON STOCK	PRICE	WON
	\$ MIL.	%	\$ MIL.	\$ MIL.	%	\$ MIL.	%	%	%	%	ENDING	EARNINGS	PER
Newmont Gold	51.7	-10	281.1	-12	29.3	-21	63.5	-20	19.3	22.0	19.4	32	1.1
Newmont Mining	50.8	-49	318.5	-9	20.0	7	59.4	-8	13.1	11.2	120.3	17	2.1
Phelps Dodge	50.0	-10	1000.4	-49	55.7	-51	133.0	-41	9.3	10.8	100.0	6	10.4
Precision Castparts	45.8	10	284.9	10	7.9	7	17.5	8	5.4	5.7	10.6	15	0.9

17 NONBANK FINANCIAL

INDUSTRY COMPOSITE	46200.9	4	91795.5	6	2497.8	15	4841.7	40	5.4	4.9	10.7	14	2.5
FINANCIAL SERVICES GROUP COMPOSITE	23725.9	8	46726.2	9	1728.8	25	3267.3	85	7.3	6.3	17.6	13	3.0
Alexander & Alexander	344.0	1	570.4	5	10.5	-24	17.0	-23	3.9	5.3	12.5	18	2.1
Allegheny	400.0	1	702.4	1	11.8	-50	14.4	-62	2.9	0.9	5.9	13	1.0
American Express	6363.0**	1	12655.0	0	257.0	-20	521.0	NM	4.0	5.3	15.1	12	2.1
Block (H&R)	716.1	28	586.2	8	154.3	17	147.8	18	21.6	22.0	32.0	23	2.6
Broad	204.9**	1	406.7	5	10.8	1	20.8	1	3.1	3.4	10.7	6	1.2
Crawford	100.0	24	265.2	20	10.1	24	18.0	19	7.5	7.5	23.9	26	1.9
Edwards (A. G.)	218.9**	32	104.8	26	23.7	65	40.8	50	10.8	8.8	10.8	13	0.9
Equifax	275.4	10	528.3	0	20.7	-3	22.4	-39	7.5	7.8	13.3	29	1.6
Federal National Mortgage Assn.	1004.0**	10	55.4.3	9	47.7	44	737.7	30	1.5	4.3	28.5	11	5.0
First Financial Management	100.0**	28	10.0	14	19.9	26	36.0	26	1.1	1.1	10.1	13	1.0
Marsh & McLennan	200.0**	1	204.3	4	81.7	0	177.3	1	1.1	1.1	28.0	19	4.1
Merrill Lynch	100.0**	1	501.0	0	84.0	149	205.0	216	0.1	2.6	12.3	11	3.8
Morgan Stanley Group	1627.5**	1	3259.3	0	101.4	74	221.0	58	6.2	4.0	17.6	10	6.8
PaineWebber Group	792.5**	1	1526.8	-2	33.8	131	65.4	157	4.3	1.9	-7.0	NM	-1.7
Primerica	1044.0**	1	3165.2	0	170.0	21	223.2	24	7.4	6.2	14.1	8	3.7
Salomon	2508.0	20	1049.0	0	78.1	48	451.0	89	7.1	5.7	14.7	9	4.0
Schwab, Charles	100.0**	10	104.8	1	4.8	48	20.1	100	5.2	3.8	17.8	25	1.0
Student Loan Marketing Assn.	100.0**	10	1000.0	0	84.7	14	100.0	10	10.0	8.0	24.4	18	3.1

INSURANCE

GROUP COMPOSITE	17151.2	3	34110.6	6	927.8	15	1731.3	11	5.4	4.9	10.6	9	4.2
Aetna Life & Casualty	4706.5	-2	9402.2	-2	159.5	-22	296.9	-23	3.4	4.2	7.3	8	4.7
American Family	783.3	26	1554.7	25	34.7	25	68.5	27	4.4	4.5	15.6	14	6.0
American National Insurance	286.6	9	583.2	10	21.0	-16	55.7	1	7.3	9.6	6.8	8	3.8
Argonaut Group	125.9	-10	270.7	-6	12.5	-42	34.9	-16	9.9	15.3	16.2	8	3.0
Berkley (W. R.)	100.0**	1	270.4	-1	1.8	-7	11.4	-17	8.6	9.3	9.0	16	1.7
Chubb	100.0**	1	144.8	0	133.0	20	261.3	18	1.1	0.8	17.1	11	0.8
Cigna	4746.0	-1	9457.0	0	170.0	0	218.0	9	3.6	3.3	6.2	8	4.0
Conseco	336.3**	-4	812.1	97	25.3	188	46.3	48	7.8	5.7	47.4	7	5.1
Hartford Steam Boiler	100.0**	1	309.1	0	4.8	0	40.0	1	3.8	14.2	20.7	15	3.7
Kemper	104.4	1	341.0	0	53.1	NM	104.0	1	6.9	NM	11.1	6	3.9
Provident Life & Accident	687.7**	-10	117.8	0	34.6	-17	70.4	-10	5.0	8.8	12.8	5	3.0
Safeco	859.6**	-4	181.4	0	51.2	-33	106.5	-20	6.0	9.6	12.3	10	4.0
St. Paul	100.0**	1	100.0	0	10.7	0	187.9	0	9.8	11.0	17.0	7	8.0
Unitrin	100.0**	1	625.7	4	19.8	-33	58.9	28	4.5	6.7	7.5	4	3.0
UNUM	591.2	0	87.0	17	55.0	0	102.6	0	9.3	9.8	10.0	11	5.7
USLife	345.2	10	659.7	0	17.9	0	33.6	7	5.2	5.7	7.8	8	4.3
Zenith National Insurance	100.4	0	104.8	0	11.0	7	22.7	0	8	8.1	-1.4	NM	-0.1

SAVINGS & LOAN

GROUP COMPOSITE	5323.7	-9	10958.7	-6	-158.7	NM	-156.9	NM	NM	NM	-8.0	NM	-1.7
Ahmanson (H. F.)	100.0**	1	1410.0	0	50.8	-1	10.0	-10	0	0.0	7.8	11	1.5
CalFed	40.0**	10	989.8	-13	-10.9	NM	-0.1	NM	NM	NM	-10.8	NM	-1.4
Citadel Holding	137.1**	1	275.7	0	7.1	4	1.8	-18	5.2	5.3	9.3	6	0.2
Coast Savings Financial	267.0**	1	512.5	-6	21.8	NM	24.7	NM	8.2	NM	-5.4	NM	-1.0
CrossLand Savings	100.0**	-38	435.3	-24	-10.1	NM	-0.0	NM	NM	NM	NM	NM	-31.1
Dime Savings Bank of N. Y.	100.0**	1	400.0	1	-0.7	NM	-35.5	NM	NM	0.0	-24.7	NM	-6.5
Glenfed	100.0**	-40	812.0	-16	-0.7	NM	-136.1	NM	NM	0.8	-23.0	NM	-8.7
Golden West Financial	100.1	0	1118.9	0	0.1	0	114.3	19	10.1	9.4	15.7	12	3.4
Great Western Financial	100.0**	-1	2047.0	0	80.2	1	104.4	-2	7.9	7.6	9.0	12	1.4
HomeFed	415.2**	-13	843.4	-12	11.5	NM	-286.4	NM	NM	NM	-73.3	NM	-21.4
Metropolitan Financial	100.0**	10	245.0	15	12.4	81	21.8	100	9.9	6.3	14.3	4	4.0
Standard Federal Bank	215.3**	-6	436.7	-4	15.4	50	28.6	47	7.2	4.3	10.0	8	1.5
TCF Financial	100.0**	-8	100.0	-8	2.6	NM	5.0	NM	2.3	NM	6.5	9	1.8

18 OFFICE EQUIPMENT & COMPUTERS

INDUSTRY COMPOSITE	46293.1	0	90332.1	2	-1210.6	NM	616.9	-86	NM	4.5	7.7	25	1.77
BUSINESS MACHINES & SERVICES GROUP COMPOSITE	3667.4	7	7356.5	9	168.3	3	308.6	-4	4.6	4.7	13.3	20	1.43
Bell & Howell	100.0**	1	300.0	0	-1.9	NM	-1.0	NM	NM	NM	-30.8	NM	-9.58
CompuCom Systems	10.0	40	202.5	14	1.0	63	1.6	52	0.9	0.8	15.3	18	0.17
CUC International	100.0**	20	252.7	14	6.5	114	12.3	10	5.0	2.9	NM	40	3.0
D-Luxe	100.0**	1	718.1	0	43.4	4	84.9	4	10.5	10.5	25.9	20	2.1
Dynalco	100.0**	0	204.0	0	6.6	-14	11.9	-24	3.4	6.4	6.2	25	1.77
HON Industries	134.8	-15	276.9	-17	5.1	-38	10.8	-48	3.8	5.2	25.5	15	1.0
Incomp Computer Centers	123.3	-9	184.1	-2	-2.4	NM	-0.9	NM	NM	1.4	4.0	25	0.29
Intelligent Electronics	421.4	22	853.1	21	10.0	55	20.5	0	2.4	1.9	28.2	9	2.4

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON EQUITY 12 MONTHS ENDING 6/30	PRICE- EARNINGS RATIO 7/26	12 MONTHS' EARNINGS PER SHARE
	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 %	2ND QUARTER 1990 %			
risel	364.8	12	729.5	38	1.5	NM	2.0	45	0.4	NM	1.1	63	0.05
roAge (3)	202.0	28	388.9	29	0.7	-50	0.9	71	0.3	0.8	12.6	9	0.94
ler (Herman) (7)	205.2	-8	412.5	-5	7.1	-48	7.7	NM	3.4	6.1	4.5	32	0.55
ey Bowes	804.0	4	1612.7	5	67.7	12	135.3	13	8.4	7.8	13.6	22	2.78
rnolds & Reynolds (3)	141.3	-5	296.0	-1	5.2	-19	10.4	-18	3.7	4.3	8.5	11	1.93
ndard Register	173.7	-3	346.0	-2	7.0	-21	12.9	-29	4.0	5.0	5.1	23	0.57
h Data (11)	126.4	25	248.5	23	2.0	63	4.2	NM	1.6	1.2	13.9	13	1.19
llace Computer Services (5)	110.3	2	232.5	3	8.7	-9	18.5	-7	7.9	8.9	12.7	13	1.79
MPUTERS & PERIPHERALS													
DUP COMPOSITE	38131.8	-2	73980.7	0	-1770.6	NM	-510.7	NM	NM	4.0	6.1	26	1.83
l International (5)	216.2	-5	425.0	-5	-1.7	NM	-0.6	NM	NM	NM	1.6	23	0.06
dahl	450.6	-13	893.3	-13	6.4	-86	17.8	-77	1.4	8.9	9.1	12	1.13
ole Computer (3)	1528.6	12	3126.3	15	-53.1	NM	78.1	-69	NM	8.8	19.6	17	2.72
olied Magnetics (3)	117.6	24	239.7	31	2.5	-17	5.3	2	2.2	3.2	5.3	16	0.56
r Research (6)	211.0	39	391.1	35	20.3	34	37.0	49	9.6	10.0	22.9	12	2.13
npaq Computer	717.8	-17	1688.6	-3	20.3	-81	134.6	-32	2.8	12.1	19.9	7	4.38
ner Peripherals	405.4	33	787.3	46	26.8	0	61.8	47	6.6	8.8	22.3	8	2.57
ntrol Data	371.3	-8	777.1	-6	5.0	-55	14.8	-18	1.3	2.8	0.2	NM	0.02
y Research	197.3	-13	340.3	-6	20.1	-53	25.3	-51	10.2	18.8	13.0	11	3.15
a General (3)	301.2	0	621.6	1	35.6	NM	54.8	NM	11.8	NM	-4.7	NM	-0.83
l Computer (11)	174.8	45	342.2	49	10.1	88	18.7	190	5.8	4.4	14.0	18	1.54
ital Equipment (6)	3944.9	17	7465.2	13	-871.3	NM	-754.7	NM	NM	NM	-8.1	NM	-5.08
atech (9)	117.0	1	230.4	-1	1.8	-58	4.2	-52	1.6	3.7	8.7	13	1.39
wlett-Packard (2)	3730.0	13	7138.0	11	233.0	25	438.0	22	6.2	5.6	11.8	16	3.32
ernational Business Machines	14732.0	11	28277.0	-8	114.0	-92	646.0	-74	0.8	8.5	10.8	14	7.38
xior (9)	234.6	59	458.1	59	-10.7	NM	-60.5	NM	NM	4.5	-49.8	NM	2.50
R	1556.0	-3	2925.0	2	99.0	-14	145.0	-13	6.4	7.2	19.6	21	5.28
antum (9)	250.9	54	542.2	85	12.5	-28	32.5	8	5.0	10.7	26.6	7	1.57
igate Technology (6)	677.0	1	1353.6	1	0.4	-99	21.1	-64	0.1	4.4	8.3	10	0.95
on Graphics (6)	165.1	37	298.2	29	9.8	-12	13.0	-35	6.0	9.3	9.7	24	1.44
rage Technology	296.0	7	578.1	8	19.9	25	34.6	38	6.7	5.8	14.6	19	2.34
dem Computers (3)	479.9	2	969.2	5	7.3	-78	25.3	-57	1.5	6.9	5.2	20	0.60
don	112.3	16	225.0	11	1.4	-78	9.2	31	1.2	6.5	22.5	9	0.33
sys	2202.8	11	4261.7	11	-1299.8	NM	-1398.0	NM	NM	0.5	NM	NM	-12.19
ing Laboratories (6)	491.4	-24	968.5	-20	-306.0	NM	-355.8	NM	NM	NM	NM	NM	-2.26
ox	4450.0**	1	8658.0	1	126.0	3	242.0	3	2.8	2.8	11.8	10	5.60
MPUTER SOFTWARE & SERVICE													
DUP COMPOSITE	4493.8	15	8994.9	17	391.6	12	818.9	13	8.7	9.0	19.0	24	1.55
ndisco (3)	517.0**	6	1097.0	14	19.0	-5	42.0	8	3.7	4.1	13.9	10	2.21
mputer Associates International (9)	263.2	3	664.3	7	3.7	2	67.9	-4	1.4	1.4	14.6	10	0.87
mputer Sciences (9)	456.4	12	932.7	13	14.4	5	35.4	-6	3.1	3.4	12.5	17	4.04
chronic Data Systems	1666.5	16	3244.6	15	139.8	12	261.6	11	8.4	8.7	22.2	22	2.19
ergraph	302.2	19	588.8	22	20.2	22	40.1	27	6.7	6.5	10.2	15	1.47
us Development	186.4	6	360.8	6	9.2	-61	15.8	-66	4.9	13.4	-2.3	NM	-0.18
icrosoft (6)	526.6	56	1013.5	56	138.4	73	262.2	69	26.3	23.7	34.3	29	2.47
vell (2)	150.2	25	284.8	26	38.4	87	68.9	93	25.6	17.1	26.2	31	1.78
icle Systems (7)	287.1	-10	556.5	0	5.5	-87	17.6	-74	1.9	13.1	-3.8	NM	-0.09
eguard Scientifics	138.3	35	251.8	28	3.0	-19	7.5	64	2.2	3.7	21.5	3	3.60
APER & FOREST PRODUCTS													
USTRY COMPOSITE	19393.5	-7	38103.5	-5	558.4	-48	1067.8	-51	2.9	5.2	6.9	22	1.94
TEST PRODUCTS													
DUP COMPOSITE	7366.1	-9	14155.1	-7	112.6	-66	140.2	-80	1.5	4.1	4.9	28	1.28
se Cascade	977.9	-7	1970.6	-7	-32.6	NM	-49.4	NM	NM	2.2	-3.6	NM	-1.17
orgia-Pacific	2981.0	-15	5759.0	-7	33.0	-69	26.0	-88	1.1	3.0	6.2	26	2.15
isiana-Pacific	485.0	-3	847.4	-13	29.2	-23	20.6	-72	6.0	7.6	3.3	41	1.03
pe & Talbot	130.7	-9	262.8	-10	1.8	-79	3.9	-80	1.4	6.0	2.0	41	0.37
yerhaeuser	2296.6	-4	4339.3	-7	69.6	-39	122.0	-50	3.0	4.8	6.9	21	1.33
llamette Industries	494.9	1	956.0	-1	11.6	-73	17.0	-80	2.3	8.9	6.2	24	2.39
PER													
DUP COMPOSITE	12027.4	-5	23948.4	-5	445.8	-39	927.6	-38	3.7	5.8	7.8	20	2.27
water	326.2	-5	650.7	-4	20.2	-13	37.0	-19	6.2	6.8	7.8	12	2.08
ampion International	1178.5	-6	2343.3	-8	4.5	-93	19.3	-86	0.4	5.0	2.2	31	0.88
esapeake	218.8	-2	417.2	-2	2.4	-68	4.8	-59	1.1	3.4	3.1	40	0.47
nsolidated Papers	221.0	-7	450.6	-6	24.6	-36	50.2	-36	11.1	16.0	12.3	15	2.62
ttfelter (P. H.)	135.1	-14	284.3	-10	17.5	-21	38.1	-10	13.0	14.2	19.7	16	3.65
ernational Paper	3100.0	-4	6197.0	-3	104.0	-44	236.0	-35	3.4	5.7	7.6	17	4.01
nes River Corp. of Virginia	1169.1	-19	2338.6	-19	22.7	-56	62.0	-39	1.9	3.6	NA	NM	0.17
nberly-Clark	1687.8	5	3355.4	5	123.2	53	243.5	23	7.3	5.0	20.9	16	5.97
ad	1176.5	-4	2273.7	-4	18.7	-65	32.1	-68	1.6	4.4	2.5	53	0.63
atch	316.6	-1	610.2	-6	11.8	-64	21.4	-69	3.7	10.1	5.6	23	1.75
tt Paper	1209.2	-8	2443.4	-6	30.5	-59	59.8	-56	2.5	5.7	3.3	41	0.99
ion Camp	730.7	2	1452.8	3	29.9	-49	71.1	-43	4.1	8.2	9.1	18	2.55
stvaco (2)	557.9	-4	1131.3	-3	35.8	-22	52.3	-43	6.4	7.9	9.0	15	2.28

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS				RETURN ON EQUITY		
	1997	1996	1995	1994	1997	1996	1995	1994	1997	1996	1995	1994	1997	1996	1995
	\$ MIL.	% CHG.	\$ MIL.	% CHG.	\$ MIL.	% CHG.	\$ MIL.	% CHG.	%	%	%	%	%	%	%
20 PUBLISHING & BROADCASTING															
INDUSTRY COMPOSITE	12730.6	0	24898.5	-1	705.5	-13	1041.0	-26	5.5	6.4	5.4	47	0.6	0.7	0.6
BROADCASTING															
GROUP COMPOSITE	2924.5	-1	5765.6	-1	230.4	-24	339.9	-33	7.9	10.2	10.5	39	1.1	1.2	1.1
American TV & Communications	308.0	10	408.7	10	38.9	37	74.0	34	12.6	10.0	10.0	32	1.1	1.1	1.1
Capital Cities/ABC	1087.8	0	2610.0	0	107.8	-10	186.4	-16	9.4	10.5	10.5	12	0.4	0.4	0.4
CBS	789.4	-14	1477.4	-10	80.7	-60	81.1	-70	7.1	16.7	17.0	10	0.1	0.1	0.1
Multimedia	104.5	9	260.8	9	14.4	14	23.4	26	10.7	10.0	10.0	20	0.1	0.1	0.1
Viacom	474.4	8	921.5	5	71.4	10	100.0	10	10.0	10.0	10.0	10	0.1	0.1	0.1
PUBLISHING															
GROUP COMPOSITE	9806.2	0	19132.9	-1	475.1	-7	701.1	-21	4.8	5.2	4.2	52	0.7	0.7	0.7
Affiliated Publications	100.9	-1	289.6	-1	2.1	-66	2.1	-66	2.4	5.6	5.9	47	0.1	0.1	0.1
Belo (A. H.)	110.9	-2	206.6	-2	3.9	-104	4.6	-90	6.6	7.6	10.4	26	0.1	0.1	0.1
Commerce Clearing House	770.0	-9	206.6	-9	2.9	-80	31.5	-14	3.4	2.9	10.0	16	0.1	0.1	0.1
Dow Jones	240.9	0	669.6	-1	24.7	-1	51.0	-10	7.6	7.9	7.0	26	0.1	0.1	0.1
Dun & Bradstreet	1160.0	-10	2088.0	-10	42.0	-5	110.7	-19	10.0	10.0	10.4	16	0.1	0.1	0.1
Gannett	374.0	-2	66.0	-2	16.0	-10	146.1	-20	10.0	10.0	10.6	26	0.1	0.1	0.1
Houghton Mifflin	1070.0	4	107.0	4	10.4	8	10.0	10.0	9.6	9.4	8.1	26	0.1	0.1	0.1
Knight-Ridder	369.5	-4	109.5	-10	9.5	-17	37.4	-9	7.0	7.5	10.0	16	0.1	0.1	0.1
McGraw-Hill	460.9	0	666.4	-1	14.9	-10	47.5	-10	7.6	8.1	10.4	16	0.1	0.1	0.1
Media General	50.0	-6	106.7	-6	1.0	-40	1.5	-20	0.4	7.6	10.6	26	0.1	0.1	0.1
Meredith	66.4	0	107.0	0	2.9	10	10.0	10.0	1.7	10.0	10.0	16	0.1	0.1	0.1
New York Times	440.4	-6	667.0	-6	3.4	-10	10.0	-10	8.0	8.7	10.0	16	0.1	0.1	0.1
Scripps (E. W.)	106.9	-1	108.4	-1	3.4	-10	14.6	-10	8.1	10.0	10.4	26	0.1	0.1	0.1
Time Warner	2680.0	10	369.0	10	10.0	10	10.0	10	10.0	10.0	10.0	10	0.1	0.1	0.1
Times Mirror	40.0	-1	106.0	-1	10.7	-10	10.0	-10	10.0	10.0	10.0	16	0.1	0.1	0.1
Tribune	309.5	-6	100.0	-10	10.7	-10	10.0	-10	10.0	10.0	10.0	16	0.1	0.1	0.1
Washington Post	100.0	-6	100.0	-10	10.7	-10	10.0	-10	10.0	10.0	10.0	16	0.1	0.1	0.1
21 SERVICE INDUSTRIES															
INDUSTRY COMPOSITE	15315.0	9	30090.3	10	653.6	-10	1204.6	-8	4.3	5.2	15.1	21	1.4	1.4	1.4
CONSTRUCTION & ENGINEERING															
GROUP COMPOSITE	3852.1	3	7765.4	5	84.6	-7	161.5	-2	2.2	2.4	13.7	22	1.6	1.6	1.6
Apogee Enterprises	10.8	6	100.0	6	1.7	-66	2.1	-16	0.0	0.0	14.4	10	0.1	0.1	0.1
EG&G	100.0	9	100.0	0	1.0	-10	10.0	-10	1.0	1.0	10.4	16	0.1	0.1	0.1
Fluor	10.0	1	100.0	1	1.0	10	10.0	10	1.0	1.0	10.0	16	0.1	0.1	0.1
Foster Wheeler	10.0	10	100.0	10	1.0	10	10.0	10	1.0	1.0	10.0	16	0.1	0.1	0.1
Jacobs Engineering Group	10.0	10	100.0	10	1.0	10	10.0	10	1.0	1.0	10.0	16	0.1	0.1	0.1
Morrison Knudsen	10.0	10	100.0	10	1.0	10	10.0	10	1.0	1.0	10.0	16	0.1	0.1	0.1
Zum Industries	10.0	10	100.0	10	1.0	10	10.0	10	1.0	1.0	10.0	16	0.1	0.1	0.1
INDUSTRIAL DISTRIBUTION															
GROUP COMPOSITE	4207.0	5	8261.0	5	120.5	-19	244.6	-13	2.9	3.7	12.7	21	1.2	1.2	1.2
AAR	10.0	-1	100.0	-1	1.0	-10	1.0	-10	0.4	0.0	7.6	16	0.1	0.1	0.1
Arrow Electronics	100.0	-4	100.0	-4	1.0	-10	1.0	-10	1.0	1.0	1.0	16	0.1	0.1	0.1
Castle (A. M.)	10.0	-4	100.0	-4	1.0	-10	1.0	-10	0.6	1.0	1.0	16	0.1	0.1	0.1
Genuine Parts	10.0	0	100.0	0	1.0	10	1.0	10	0.6	0.6	10.4	16	0.1	0.1	0.1
Gerry Petroleum	10.0	0	100.0	0	1.0	10	1.0	10	1.0	1.0	1.0	16	0.1	0.1	0.1
Granger (W. W.)	10.0	0	100.0	0	1.0	10	1.0	10	1.0	1.0	1.0	16	0.1	0.1	0.1
Howe	10.0	0	100.0	0	1.0	10	1.0	10	1.0	1.0	1.0	16	0.1	0.1	0.1
Kaman	10.0	-1	100.0	-1	1.0	-10	1.0	-10	1.0	1.0	1.0	16	0.1	0.1	0.1
Marshall Industries	10.0	-4	100.0	-4	1.0	-10	1.0	-10	1.0	1.0	1.0	16	0.1	0.1	0.1
MLX	10.0	-1	100.0	-1	1.0	-10	1.0	-10	1.0	1.0	1.0	16	0.1	0.1	0.1
Office Depot	10.0	0	100.0	0	1.0	10	1.0	10	1.0	1.0	1.0	16	0.1	0.1	0.1
Premier Industries	10.0	-1	100.0	-1	1.0	-10	1.0	-10	1.0	1.0	1.0	16	0.1	0.1	0.1
TBC	10.0	0	100.0	0	1.0	10	1.0	10	1.0	1.0	1.0	16	0.1	0.1	0.1
United Stationers	10.0	-1	100.0	-1	1.0	-10	1.0	-10	1.0	1.0	1.0	16	0.1	0.1	0.1
Univar	10.0	0	100.0	0	1.0	10	1.0	10	1.0	1.0	1.0	16	0.1	0.1	0.1
Willcoxon & Gibbs	10.0	0	100.0	0	1.0	10	1.0	10	1.0	1.0	1.0	16	0.1	0.1	0.1
Wyle Laboratories	10.0	0	100.0	0	1.0	10	1.0	10	1.0	1.0	1.0	16	0.1	0.1	0.1
POLLUTION CONTROL															
GROUP COMPOSITE	3191.6	24	6164.8	27	273.5	-11	518.4	-7	8.6	11.9	17.9	23	1.2	1.2	1.2
Air & Water Technologies	10.0	0	100.0	0	1.0	10	1.0	10	1.0	1.0	1.0	16	0.1	0.1	0.1
Browning-Ferris Industries	10.0	0	100.0	0	1.0	10	1.0	10	1.0	1.0	1.0	16	0.1	0.1	0.1
Chemical Waste Management	10.0	0	100.0	0	1.0	10	1.0	10	1.0	1.0	1.0	16	0.1	0.1	0.1
Waste Management	10.0	0	100.0	0	1.0	10	1.0	10	1.0	1.0	1.0	16	0.1	0.1	0.1
PRINTING & ADVERTISING															
GROUP COMPOSITE	1649.8	17	3173.8	17	93.7	-2	138.3	-11	5.7	6.8	14.2	17	2.3	2.3	2.3
Adva-System	10.0	0	100.0	0	1.0	10	1.0	10	1.0	1.0	1.0	16	0.1	0.1	0.1
Bentley	10.0	-1	100.0	-1	1.0	-10	1.0	-10	1.0	1.0	1.0	16	0.1	0.1	0.1
Donnelley (R. R.) & Sons	10.0	0	100.0	0	1.0	10	1.0	10	1.0	1.0	1.0	16	0.1	0.1	0.1
Interpublic Group	10.0	0	100.0	0	1.0	10	1.0	10	1.0	1.0	1.0	16	0.1	0.1	0.1

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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS				RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE-EARNINGS RATIO 7-26	12 MONTH EARNINGS PER SHARE
	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 %	2ND QUARTER 1990 %					
(e) OTHER SERVICES															
GROUP COMPOSITE	2414.6	6	4725.2	7	81.4	-6	141.8	-10	3.4	3.8	14.3	20	1.30		
Adia Services	159.8**	-4	314.5	-4	2.0	-61	3.3	-67	1.2	3.0	5.9	25	0.8		
American Building Maintenance (2)	180.8	10	358.4	9	2.5	13	4.4	13	1.4	1.4	12.8	13	2.5		
JWP	757.9	11	1486.9	14	14.8	3	28.9	6	2.0	2.1	15.7	10	1.6		
Kelly Services	347.1	-6	677.5	-6	9.7	-47	18.2	-47	2.8	4.9	16.4	19	1.8		
Pinkerton's	142.3	6	283.5	6	2.8	24	4.2	41	1.9	1.7	23.7	17	1.6		
Rollins	135.6	10	240.2	9	13.6	12	17.6	12	10.0	9.8	29.9	20	1.2		
Safety-Kleen	159.1	20	312.3	21	13.0	8	24.4	5	8.2	9.0	13.1	32	1.0		
Service Corp. International	156.1	12	309.6	7	16.3	4	35.0	-1	10.4	11.3	13.9	20	1.3		
ValCom	122.0	26	235.9	19	0.8	-50	2.1	-36	0.7	1.7	14.4	8	1.4		
Volt Information Sciences (2)	114.0	-15	221.6	-10	3.9	305	0.2	NM	3.4	0.7	1.0	65	0.1		
Wackenhut	139.8	9	284.7	12	1.9	10	3.5	15	1.4	1.4	19.2	15	1.9		
22 TELECOMMUNICATIONS															
INDUSTRY COMPOSITE	41222.2	3	81319.3	3	3766.3	1	7134.5	-4	9.1	9.4	13.6	15	2.60		
(a) EQUIPMENT & SERVICES															
GROUP COMPOSITE	14255.1	7	28076.5	6	1065.8	16	2032.1	6	7.5	6.9	16.4	17	2.11		
American Telephone & Telegraph	9525.0	5	18717.0	4	828.0	26	1540.0	16	8.7	7.3	19.3	15	2.60		
Communications Satellite	127.6	9	254.5	12	19.4	4	37.9	1	15.2	16.0	-2.8	NM	-0.90		
DSC Communications	116.9	-5	250.7	6	-25.7	NM	-21.6	NM	NM	7.2	-6.0	NM	-0.30		
MCI Communications	2098.0	12	4123.0	12	137.0	-23	267.0	-21	6.5	9.5	7.9	37	0.70		
Pacific Telecom	180.3	26	362.4	28	18.0	-5	36.2	-25	10.0	13.3	14.6	13	2.10		
United Telecommunications	2207.2	7	4368.9	7	89.0	119	172.6	16	4.0	2.0	14.0	17	1.50		
(b) TELEPHONE COMPANIES															
GROUP COMPOSITE	26967.2	1	53242.9	1	2700.5	-4	5102.4	-7	10.0	10.6	12.8	15	2.92		
Alltel	439.9	13	851.7	10	46.9	5	93.7	4	10.7	11.5	18.8	16	2.40		
Ameritech	2742.1	2	5370.6	1	303.9	-14	586.9	-11	11.1	13.1	15.1	13	4.40		
Bell Atlantic	3081.4	0	6077.1	0	355.1	-2	708.7	-1	11.5	11.8	14.4	14	3.30		
BellSouth	3582.6	-1	7122.5	0	365.3	-18	767.6	-12	10.2	12.3	11.9	15	3.10		
Centel	298.9	0	586.5	1	53.0	368	57.7	141	17.7	3.8	7.5	33	0.90		
Cincinnati Bell	256.3	5	531.0	14	-7.9	NM	7.6	-82	NM	9.7	8.9	22	0.80		
GTE	5367.0	1	10591.0	0	403.0	0	603.0	-26	7.5	7.6	13.5	16	1.80		
Nynex	3361.0	-2	6717.4	-1	290.8	-3	560.3	-5	8.7	8.7	9.9	16	4.50		
Pacific Telesis Group	2520.0	4	4930.0	3	316.0	10	582.0	6	12.5	11.8	14.0	16	2.60		
Rochester Telephone	162.7	12	322.1	10	27.9	133	40.8	69	17.1	8.2	14.4	13	2.20		
Southern New England Telecomms.	411.5**	2	806.3	0	16.7	-55	54.3	-28	4.1	9.1	9.7	17	1.80		
Southwestern Bell	2242.5	3	4385.7	2	253.3	-4	477.2	-6	11.3	12.1	12.4	15	3.50		
US West	2501.2	4	4951.0	2	276.6	0	562.5	3	11.1	11.5	12.8	11	3.00		
23 TRANSPORTATION															
INDUSTRY COMPOSITE	27329.7	3	53016.8	3	290.1	-73	-68.8	NM	1.1	4.1	1.2	NM	0.32		
(a) AIRLINES															
GROUP COMPOSITE	11319.0	7	21414.8	6	9.5	-97	-664.0	NM	0.1	3.0	-16.0	NM	-6.13		
Alaska Air Group	278.3	6	525.0	6	4.5	-53	-5.5	NM	1.6	3.6	-0.9	NM	-0.22		
America West Airlines	378.5	16	731.4	16	-30.9	NM	-80.8	NM	NM	1.5	NM	NM	-8.30		
AMR	3194.5	7	5964.1	5	10.3	-92	-185.3	NM	0.3	4.3	-8.7	NM	-5.16		
Delta Air Lines (6)	2524.1	13	4823.4	11	19.2	-74	-64.9	NM	0.8	3.3	-17.4	NM	-7.70		
Southwest Airlines	324.7	5	607.5	7	10.6	-55	2.4	-92	3.3	7.6	3.5	53	0.40		
UAL	2954.2	8	5516.9	5	52.7	-65	-104.3	NM	1.8	5.4	-6.9	NM	-5.36		
USAir Group	1664.8	-3	3246.5	0	-56.8	NM	-225.5	NM	NM	NM	-47.7	NM	-13.28		
(b) RAILROADS															
GROUP COMPOSITE	7718.4	-1	15289.0	-1	96.0	-83	438.2	-51	1.2	7.3	8.3	19	2.23		
Burlington Northern	1080.0	-8	2212.0	-6	-420.0	NM	-428.0	NM	NM	6.1	-27.5	NM	-4.36		
Consolidated Rail	811.0	-6	1566.0	-7	73.0	-1	91.0	-8	9.0	8.6	8.5	12	5.39		
CSX	2125.0	4	4155.0	5	115.0	6	172.0	27	5.4	5.3	10.9	12	4.05		
Illinois Central	131.3	-5	269.3	-6	13.7	23	29.0	16	10.4	8.1	33.8	11	2.06		
Kansas City Southern Industries	149.7**	18	292.3	15	10.1	16	19.7	8	6.7	6.9	11.3	13	4.09		
Norfolk Southern	1110.0	-6	2175.3	-6	134.0	-14	234.0	-21	12.1	13.2	10.3	15	3.19		
Santa Fe Pacific	569.4	5	1134.1	-2	17.2	NM	34.5	NM	3.0	NM	1.2	NM	0.07		
Union Pacific	1742.0	1	3485.0	3	153.0	0	286.0	2	8.8	8.9	14.3	14	6.21		
(c) TRANSPORTATION SERVICES															
GROUP COMPOSITE	4495.9	2	8780.7	3	86.4	-24	3.4	-98	1.9	2.6	4.4	30	0.93		
Airborne Freight	339.4	17	657.8	17	10.3	-4	14.9	-13	3.0	3.7	10.8	19	1.51		
Federal Express (7)	1914.2	0	3778.7	4	31.0	-28	-74.6	NM	1.6	2.3	0.4	NM	0.11		
Harper Group	113.1	0	224.8	5	4.9	3	8.8	-2	4.3	4.2	14.0	14	1.80		
HH (8)	546.3	6	1035.3	5	12.7	-21	24.7	-21	2.3	3.1	12.0	11	2.78		
Ryder System	1282.9	-1	2483.2	-2	21.6	-35	19.4	-53	1.7	2.6	3.8	27	0.68		
Trinity Industries (9)	300.0	6	600.9	-3	5.9	0	10.3	-10	2.0	2.1	8.9	17	1.43		

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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS				RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE- EARNINGS RATIO 7-26	12 MONTHS' EARNINGS PER SHARE
	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990	2ND QUARTER 1991 %	2ND QUARTER 1990 %					
TRUCKING & SHIPPING															
GROUP COMPOSITE	3796.4	4	7532.4	3	98.3	14	153.6	0	2.6	2.4	7.0	23	1.28		
Alexander & Baldwin	189.7**	11	353.5	-6	24.8	11	38.4	-45	13.1	13.1	12.2	13	1.82		
American President	551.3**	8	1175.5	7	11.2	647	19.1	NM	2.0	0.3	-11.2	NM	-2.27		
Arline Freight	176.8	6	343.9	5	2.0	NM	0.7	980	1.1	NM	2.3	38	0.45		
Consolidated Freightways	1013.1	-3	2059.6	1	-7.0	NM	-18.1	NM	NM	NM	-3.7	NM	-0.61		
Exxon	242.6**	14	454.4	13	20.6	15	39.5	5	8.5	8.4	12.7	10	3.69		
Frontier (J. B.) Transport Services	166.6	18	325.1	17	7.8	-8	11.7	-20	4.7	6.0	14.0	19	1.17		
Genstar	144.7	-14	280.3	-15	1.9	52	1.2	13	1.3	0.7	-21.4	NM	-3.23		
Greyhound Lines	711.5	6	1379.2	5	25.7	13	44.3	13	3.6	3.4	15.2	15	3.19		
Low Freight System	600.2	5	1161.0	2	11.3	-32	16.8	-44	1.9	2.9	11.2	16	1.86		
UTILITIES & POWER															
GROUP COMPOSITE	46330.5	8	98909.0	6	3857.7	26	8537.8	8	8.3	7.1	9.7	13	2.10		
ELECTRIC, WATER & COGENERATION															
GROUP COMPOSITE	38422.0	7	78652.1	6	3812.9	31	7700.9	10	9.9	8.1	10.0	13	2.18		
Allegheny Power System	547.9	0	1144.7	-3	45.8	5	110.4	-1	8.4	7.9	11.5	11	3.55		
American Electric Power	1231.0	-2	2488.4	-3	114.8	-9	273.9	-4	9.3	10.0	11.6	11	2.63		
Atmos Energy	558.2	16	1150.1	12	59.2	52	100.3	33	10.6	8.1	7.6	16	1.88		
Edison	290.0	8	597.7	3	4.6	NM	13.1	3	1.6	NM	8.3	12	1.60		
Florida Power & Light	636.2	5	1273.0	5	74.9	587	165.4	66	11.8	1.8	13.9	11	4.11		
Interior Energy	627.4	9	1216.1	7	66.7	-6	105.3	-23	10.6	12.2	8.6	9	1.78		
Norfolk & South West	717.0	10	1365.0	13	94.0	59	157.0	-18	13.1	9.1	11.9	13	3.44		
Norfolk Maine Power	199.7	5	424.3	8	15.5	131	31.7	28	7.8	3.5	10.7	10	1.78		
PG&E	128.5	8	287.9	12	8.4	-14	20.4	12	6.5	8.2	11.5	12	2.88		
Pennsylvania Gas & Electric	328.4	4	772.0	8	37.3	-12	121.5	14	11.4	13.4	15.5	8	4.27		
PG&E	146.7	3	313.4	9	16.8	26	28.2	31	11.4	9.3	12.2	12	2.12		
PG&E	635.0	-1	1612.0	7	32.6	-34	-171.4	NM	5.1	7.7	-69.8	NM	-10.12		
Commonwealth Edison	1521.4	78	2839.7	27	157.5	NM	162.3	NM	10.4	NM	8.1	16	2.36		
Commonwealth Energy System	199.7	16	450.9	9	0.3	NM	18.3	28	0.2	NM	7.9	13	2.56		
Consolidated Edison Co. of N. Y.	1330.6	5	2810.0	2	64.7	32	171.3	-8	4.9	3.9	11.5	11	2.27		
Imperial Power & Light	195.8	6	414.6	3	13.0	6	38.0	3	6.6	6.6	4.8	31	0.62		
Metro Edison	877.4	10	1698.8	5	135.5	15	268.6	6	15.4	14.8	18.7	9	3.37		
Minion Resources	901.2**	8	1805.4	6	103.0	3	220.7	-9	11.4	12.0	11.6	12	4.14		
PG&E	226.8	8	517.3	7	22.0	-39	84.0	-5	9.7	17.1	13.5	10	2.15		
PG&E	288.9	6	578.0	4	32.7	30	68.8	10	11.3	9.3	11.8	11	2.40		
PG&E	893.6	3	1780.3	3	138.4	18	275.8	13	15.5	13.4	13.4	11	2.54		
PG&E	981.4	4	1874.3	3	96.8	-23	197.0	-14	9.9	13.3	11.0	10	2.39		
PG&E	528.1	8	984.7	5	47.3	-2	84.5	3	9.0	9.9	12.8	12	3.51		
PG&E	1388.7	9	2551.9	9	85.6	-20	167.6	8	6.2	8.5	-12.6	15	2.04		
General Public Utilities	781.6	12	1594.7	10	66.1	9	153.2	5	8.5	8.7	12.4	10	2.55		
Idaho States Utilities	420.0	1	810.5	2	10.8	NM	35.2	NM	2.6	NM	1.9	32	0.33		
Idaho States Electric Industries	260.5	2	547.2	11	14.8	-5	29.3	2	5.7	6.1	8.6	16	2.02		
Idaho Power	110.9	1	231.5	5	10.0	-30	25.8	-17	9.0	12.9	10.4	14	1.76		
Illinois Power	310.7	2	669.5	8	19.2	424	28.1	NM	6.2	1.2	-5.4	NM	-0.99		
Illinois Gas & Electric	110.7	4	247.9	2	14.2	19	26.7	25	12.8	11.2	13.3	11	2.16		
Illinois Enterprises	153.1	5	313.4	6	23.0	-6	50.1	-3	15.0	16.8	12.9	11	2.57		
Illinois Power & Light	220.7	-10	643.6	-4	4.8	-48	38.0	-3	2.2	3.8	11.8	11	2.20		
Kentucky Utilities	142.4	9	289.1	10	18.0	10	42.6	11	12.7	12.6	14.4	11	2.11		
Kentucky Energy	161.3	2	356.3	4	19.1	6	43.7	20	11.9	11.4	12.2	11	3.75		
Kentucky Island Lighting	541.4	6	1208.7	3	50.1	5	136.5	8	9.3	9.4	12.5	10	2.36		
Kentucky Resources	229.1	21	486.5	10	12.6	8	34.0	18	5.5	6.1	10.8	15	1.35		
Minnesota Power & Light	120.1	4	245.8	2	13.3	-24	30.9	-17	11.1	15.1	12.6	13	2.10		
Montana Power	198.6**	11	462.0	11	10.5	-19	53.3	12	5.3	7.2	11.9	11	1.94		
New England Electric System	456.9	7	1013.7	12	22.0	10	98.2	36	4.8	4.7	20.1	7	4.47		
New York State Electric & Gas	373.4	2	816.9	1	43.1	-1	116.3	2	11.5	11.8	10.3	11	2.37		
Ontario Mohawk Power	807.0	9	1799.5	6	57.7	61	167.5	31	7.1	4.8	4.0	27	0.60		
PG&E	320.4	-2	782.7	0	23.3	10	72.3	8	7.3	6.5	13.1	11	1.90		
PG&E	637.0	6	1338.3	4	62.0	19	141.9	9	9.7	8.7	12.3	10	2.04		
PG&E	501.5	6	1078.5	4	24.6	-31	80.5	-12	4.9	7.6	10.6	13	2.62		
PG&E	564.2	8	1152.6	6	68.7	-20	143.4	-23	12.2	16.4	8.5	13	1.41		
PG&E	329.4	9	603.6	7	33.5	1	46.4	2	10.2	10.9	15.8	11	3.42		
PG&E	131.6	6	294.9	6	7.2	2	20.2	19	5.5	5.7	12.4	10	3.77		
PG&E	2351.9	8	4622.8	5	305.5	84	444.9	18	13.0	7.7	13.0	11	2.29		
Pennsylvania Power & Light	593.8	6	1258.7	6	72.5	8	182.9	5	12.2	12.0	13.6	11	4.06		
Philadelphia Electric	958.6	12	1948.4	9	125.0	-8	268.9	358	13.0	15.8	6.9	18	1.11		
Piedmont West Capital	362.5	-13	694.8	-9	22.5	126	35.9	16	6.2	2.4	4.9	13	0.86		
Piedmont General	200.6	9	434.0	2	8.4	50	43.3	-5	4.2	3.0	12.4	8	2.12		
PG&E	361.1	16	650.6	9	42.8	42	49.7	37	11.8	9.6	11.4	13	1.70		
PG&E	251.0	6	508.4	4	28.6	9	64.2	-4	11.4	11.1	17.6	7	2.14		
PG&E	390.7	-7	941.6	1	12.2	-60	57.3	-21	3.1	7.2	12.0	11	2.18		
PG&E	190.4	-3	433.9	-4	-1.6	NM	11.6	NM	NM	NM	1.1	51	0.19		
PG&E	1151.0	7	2567.3	7	129.5	23	297.5	16	11.3	9.8	12.5	10	2.68		
PG&E	216.8	4	492.9	4	24.8	-6	81.3	6	11.4	12.6	13.2	10	2.26		
PG&E	182.6	0	428.3	1	1.5	-26	25.8	-1	0.8	1.1	9.0	12	1.70		
PG&E	406.8	1	854.8	1	53.6	9	107.0	2	13.2	12.1	15.1	11	3.56		

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS				RETURN ON COMMON EQUITY 12 MONTHS ENDING 6-30	PRICE- EARNINGS RATIO 7-26	1 MON EARN PER SH
	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 \$ MIL	CHANGE FROM 1990 %	6 MONTHS 1991 \$ MIL	CHANGE FROM 1990 %	2ND QUARTER 1991 %	2ND QUARTER 1990 %					
Scana	256.2	2	553.9	1	26.0	-9	66.3	3	10.2	10.9	18.1	8	4.3		
SCEcorp	1695.1	6	3365.1	6	178.2	13	360.7	6	10.5	9.9	14.6	11	3.7		
Sierra Pacific Resources	110.7	1	239.3	0	8.0	-2	22.8	-7	7.3	7.4	11.3	12	1.8		
Southern	2015.4	0	3798.6	3	197.7	-19	362.0	-7	9.8	12.1	8.6	15	1.8		
Southwestern Public Service (4)	172.0	-3	339.2	-5	24.1	3	48.2	4	14.0	13.2	16.0	11	2.9		
Teco Energy	290.9	5	543.5	6	38.6	-2	65.9	-3	13.3	14.1	16.5	14	2.4		
Texas Utilities	1197.4	15	2291.9	16	180.8	-28	335.3	-28	15.1	24.1	10.1	10	3.9		
Union Electric	555.0	11	992.5	5	105.2	27	140.3	13	19.0	16.5	14.8	11	2.5		
United Illuminating	142.5	11	312.3	14	9.7	2	29.4	55	6.8	7.4	15.3	8	4.3		
UtiliCorp United	189.4	17	506.0	9	6.3	31	34.9	26	3.3	3.0	11.4	11	2.1		
Washington Water Power	123.9	-3	285.2	1	19.3	2	45.2	0	15.6	14.8	12.3	11	2.7		
Wheelabrator Technologies	290.6	0	552.6	0	48.3	182	67.9	116	16.6	5.9	14.3	25	1.0		
Wisconsin Energy	355.2	5	772.9	6	38.3	-4	94.1	-1	10.8	11.8	13.2	12	2.7		
WPL Holdings	147.9	7	324.9	5	11.3	12	31.1	1	7.6	7.3	13.5	12	2.2		
(b) GAS, OIL & TRANSMISSION															
GROUP COMPOSITE	7908.5	10	20256.8	7	44.9	-70	836.9	-6	0.6	2.1	6.3	23	1.2		
Arkla	533.3**	11	1543.5	28	-29.2	NM	31.3	-51	NM	1.6	5.5	NA	NM		
Brooklyn Union Gas (3)	164.7	-4	567.6	6	-7.4	NM	54.7	-2	NM	NM	8.5	14	2.1		
Consolidated Natural Gas	424.3	-6	1481.8	-3	-5.4	NM	95.9	2	NM	0.5	8.7	21	1.5		
Eastern Enterprises	227.1	1	555.9	6	2.1	-89	29.9	-40	0.9	8.1	8.3	12	1.5		
Enron	3035.4	35	6642.5	25	37.6	11	146.4	9	1.2	1.5	11.3	17	3.7		
Enserch	609.7	0	1417.1	3	-12.7	NM	28.4	-44	NM	0.9	6.0	25	0.6		
National Fuel Gas (3)	146.7	-6	484.5	-1	-1.2	NM	34.8	-2	NM	NM	8.5	15	1.6		
Nicor	233.1	-13	876.8	-3	15.5	-24	62.7	-2	6.7	7.6	15.6	11	3.8		
Oneok (4)	146.5	6	426.3	1	3.6	-57	31.6	-1	2.5	5.4	8.6	12	1.1		
Panhandle Eastern	480.2	-3	1319.5	-18	-1.8	NM	38.9	24	NM	NM	-19.3	NM	-2.5		
Peoples Energy (3)	170.8	-16	660.3	0	2.5	-72	51.8	5	1.5	4.5	10.0	15	1.8		
Piedmont Natural Gas (2)	141.8	6	297.8	-1	15.3	4	32.4	-15	10.8	11.0	7.7	16	1.8		
Questar	133.0	31	369.3	22	8.6	97	41.4	25	6.5	4.3	13.4	12	1.6		
Sonat	312.4	2	841.3	11	9.5	-39	57.7	20	3.1	5.1	10.1	15	2.8		
Transco Energy	572.1	-16	1341.6	-18	-4.4	NM	23.8	-54	NM	3.1	-2.0	NM	-0.4		
Wicor	129.3	-7	375.5	0	-1.7	NM	18.3	2	NM	0.7	6.0	21	1.0		
Williams	448.0	17	1055.6	13	14.0	73	56.8	42	3.1	2.1	7.9	18	1.9		

ALPHABETICAL LIST OF COMPANIES

The number following each company name identifies the Scoreboard category under which it is listed

A	American Electric 24a	Atlantic Richfield 11b	Big B 12a	Carolina Power 24a	Coastal 11b	Crawford 17a	Dominion Bankshare
A&P 10c	American Express 17a	AutoZone 8	Bindley Western 12a	Carpenter Tech. 16b	Coca-Cola 6c	Gray Research 18b	Dammon Resources
AAK 21b	American Family 17b	Avery Dennison 15a	Black & Decker 15b	Carter Hawley Hale 8	Coca-Cola Bottling 6c	Crestar Financial 3c	Donaldson 2b
Abbott Laboratories 12d	American Greetings 14d	Avon Products 6d	Blair 8	Carter-Wallace 12b	Coca-Cola Enterprises 6c	Crompton & Knowles 4	Dannely (R. R.) 21
Academy Sports 21e	American Home 12b	Aztec 14c	Black (H&R) 17a	Casey's General 10b	Colgate-Palmolive 6d	Crossland Savings 17c	Dover 15c
Advanced Micro 9d	American Maize 10b		Black Drug 6d	Castle (A. M.) 21b	Comdisco 18c	Crown Central 11b	Dow Chemical 4
Advo System 21d	American Medical 12c		Blackbuster Ent 14b	Castle & Cooke 10b	Comerica 3b	Crown Cork & Seal 7a	Dow Jones 20b
Advo Tube & Capacity 17b	American National 17b		Blount 15a	Caterpillar 15c	Commerce Clearing 20b	Crystal Brands 6a	DPI 24a
Affiliated Pubs 20b	American President 23d		Boatmen's Bancshares 3b	CBS 20a	Commercial Metals 16b	CSX 23b	DQE 24a
Africanus H. F. 17c	American Stores 10c		Bob Evans Farms 14a	Centel 22b	Commonwealth Ed 24a	CUC International 18a	Dresser Industries 11
Air & Water Tech. 21c	American TV 20a		Boeing 1	Center Energy 24a	Comm. Energy 24a	Cummins Engine 2b	Drug Emporium 12c
Air Products & Chemicals 4	Ameritech 22b		Boise-Cascade 19a	Centex 13b	Commtron 14b	Cyprus Industries 16b	DSC Communs 22c
Airborne Freight 23c	Ameritrust 3b		Borden 10b	Central & South West 24a	Community Psych. 12c	Cyprus Minerals 16c	Du Pont 4
Alaska Air Group 23a	Ameron 13a		Boston Edison 24a	Central Maine Power 24a	Compaq Computer 18b		Duke Power 24a
Albany International 15d	Ames Dept. Stores 8		Bowater 19b	Champion Intl 19b	ComuCom Systems 18a		Dun & Bradstreet 20
Alberto-Culver 6d	Amgen 12b		Bristol-Myers Squibb 12b	Charming Shoppes 8	Computer Associates 18c		Durr-Fillauer Medica
Albertson's 10c	Amoco 11b		Broad 17a	Chase Manhattan 3a	Computer Science 18c	Dairy Mart 10c	DWG 15d
Alco Standard 5	AMP 9d		Brown Group 6a	Chemical Bank 3a	Comsat 22a	Dana 2b	Dynatech 18b
Alcoa 16a	AMR 23a		Brown-Forman 6c	Chemical Waste 21c	ConAgra 10b	Danaher 15b	
Alexander & Alex 17a	Analog Devices 9d		Browning-Ferris 21c	Chesapeake 19b	Conner Peripherals 18b	Dart Group 5	
Alexander & Baldwin 23d	Anheuser-Busch 6c		Brunswick 14d	Chevron 11b	Consco 17b	Data General 18b	E-Systems 9b
Allegheny 17a	Ant-Taylor Stores 8		Burlington Northern 23b	Chrysler 2a	Consolidated Edison 24a	Dayton Hudson 8	Eagle Food Centers
Allegheny Ludlum 16b	Apogee Enterprises 21a		BWIP 15c	Church & Dwight 6d	Cons. Freightways 23d	Dean Foods 10b	Eagle-Picher Industr
Allegheny Power 24a	Apple Computer 18b			Cigna 17b	Cons. Natural Gas 24b	Deere 15c	Eastern Enterprises 2
Allergan 12b	Applied Magnetics 18b			Cilcorp 24a	Consolidated Papers 19b	Dell Computer 18b	Eastman Kodak 14c
Alliant Techsystems 15a	Applied Materials 15c			Cincinnati Bell 22b	Consolidated Rail 23b	Delta Air Lines 23a	Eaton 2b
Allied Signal 5	Arco Chemical 4			Cincinnati G&E 24a	Consolidated Stores 8	Deluxe 18a	Echlin 2b
Alltel 22b	Argonaut Group 17b			Cincinnati Milacron 15b	Constar International 7a	Detroit Edison 24a	Eckerd (Jack) 12a
AM International 18b	Arkla 24b			Cipco 22a	Continental Bank 3b	Dexter 4	Ecolab 6d
Amax 16a	Armco 16b			Circuit City Stores 6b	Control Data 18b	Dial 5	Edison Brothers 8
Amco 18b	Armstrong World 6b			Circuit City Stores 6b	Cooper Industries 9a	Diamond Shamrock 11b	Edwards (A. G.) 17a
Amerasia Hess 11b	Arrow Electronics 21b			Circuit City Stores 6b	Coors (Adolph) 6c	Diebold 18a	EG&G 21a
Amerasia West 23a	Arvin Industries 2b			Circuit City Stores 6b	CorkStates Financial 3a	Digital Equipment 18b	Electronic Data 18c
American Building 21e	Ashland Oil 11b			Circuit City Stores 6b	Costco Wholesale 8	Dillard's 8	Engelhard 4
American Can 4	A.T. Research 18b			Circuit City Stores 6b	CPC International 10b	Dime Savings Bank 17c	Enron 24b
	AT&T 22a			Circuit City Stores 6b	Crane 15a	Disney (Walt) 14b	Enserch 24b
						Dollar General 8	Entergy 24a

Continued on

THE ONLY YARDSTICK THAT COUNTS.

Much has been written about various ways
to measure corporate performance. But over the years, the
odds-on favorite would have to be earnings.

We think that a focus on earnings misses
a much more relevant factor

Free cash flow.

And once again, we expect ours to remain strong.
Extremely strong. In fact, in a year when business has certainly
not been booming, our free cash flow will run close to
\$1 billion. And we expect that number to average substantially
more in the coming years.

And the point?

Cash, not earnings, has put us on the fast track to debt reduction.

In fact, between cash from operations and the sales of
certain non-strategic assets, we're well ahead of schedule. Which
means we're adding economic value to the company
more quickly than many thought we could.

To be sure, there are as many opinions on the subject
of how best to judge value as there are people to pen them.
But we think we'll stick with cash. It sure works for us.

And we think it works for our shareholders.

Georgia-Pacific



CORPORATE SCOREBOARD

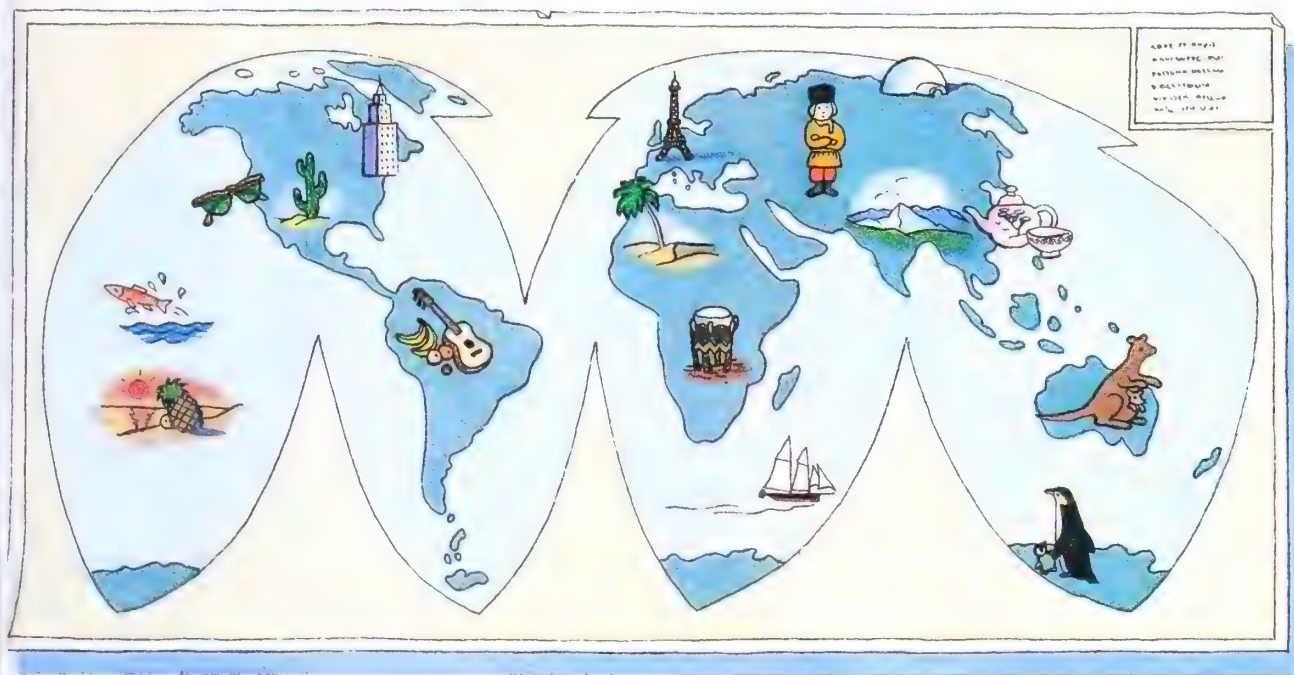
ALPHABETICAL LIST OF COMPANIES

The number following each company name identifies the Scoreboard category under which it is listed

Continued from p. 74 Equifax 17a Ethyl 4 Exxon 11b	GTE 22b Gulf States Utilities 24a	K K mart 8 Kamau 21b Kansas City Southern 23b Kansas Power 24a Karcher (Carl) 14a Kaufman & Broad 13b Kellogg 10b Kellwood 6a Kelly Services 21e Kemper 17b Kennametal 15b Kentucky Utilities 24a Kerr-McGee 11b KeyCorp 3a Keystone Intl. 15a Kimberly-Clark 19b Knight-Ridder 20b Kroger 10c	Media General 20b Medtronic 12d Mellon Bank 3a Melville 8 Mercantile Stores 8 Merck 12b Meredith 20b Meridian Bancorp 3a Merisel 18a Merrill Lynch 17a Merry-Go-Round 8 Metropolitan Fincl. 17c Meyer (Fred) 8 Michael Foods 10b Michigan National 3b MicroAge 18a Micron Technology 9d Microsoft 18c Midatlantic 3a Midwest Resources 24a Miller (Herman) 18a Millipore 9c Mine Safety 12d Minnesota Mining 15a Minnesota Power 24a Mitchell Energy 11b MLX 21b MNC Financial 3a Mobil 11b Modine Mfg 2b Monsanto 4 Montana Power 24a Morgan (J. P.) 3a Morgan Stanley 17a Morrison 14a Morrison Knudsen 21a Morton International 4 Motorola 9b Multimedia 20a	Office Depot 21b Ohio Edison 24a Oklahoma G&E 24a Olin 4 Oneok 24b Oracle Systems 18c Orange & Rockland 24a Oregon Steel 16b Orion Pictures 14b Oryx Energy 11b Outboard Marine 14d Owens & Minor 12d Owens-Corning 13a Oxford Industries 6a	Quantum 18b Quantum Chemical 4 Questar 24a QVC Network 8	R Ralston Purina 10b Raychem 9a Raytheon 9b Reebok International 6a Republic Health 12c Republic New York 3a Rexene 4 Reynolds & Reynolds 18a Reynolds Metals 16a Rhone-Poulenc Rorer 12b Richford Holdings 10a Rite Aid 12a RJR Nabisco 6c Roadway Services 23d Robertson Ceko 15a Rochester G&E 24a Rochester Telephone 22b Rockwell International 5 Rohm & Haas 4 Rohr Industries 1 Rollins 21e Rose's Stores 8 Ross Stores 8 RPM 13a Rubbermaid 15a Ruddick 10c Russell 6a Ryder System 23c Rykooff-Sexton 10a Ryland Group 13b	Southwestern PS 24a Spiegel 8 Springs Industries 15d SPX 15b St. Paul 17b Standard Federal 17c Standard Motor 2b Standard Products 2b Standard Register 18a Stanhome 6d Stanley Works 15b State Street Boston 3a Sterling Chemicals 4 Stewart & Stevenson 15c Stone Container 7b Stop & Shop 10c Storage Technology 18b Strawbridge & Clothier 8 Stride Rite 6a Student Loan Mktg. 17a Sun 11b Sundstrand 1 SunTrust Banks 3c Super Food Services 10a Super Valu Stores 10a Supermarkets Gen. 10c Syntex 12b	United Illuminating 2 United Stationers 21 United Technologies 2 United Telecomms. 2 Unitrin 17b Univar 21b Universal Foods 10b Universal Health 12c Unocal 11b Unocal Exploration 1 UNUM 17b Upjohn 12b US West 22b USAir Group 23a USC 13a USLife 17b USX-Marathon 11b USX-U. S. Steel 16b UnihCorp United 24c			
F Family Dollar Stores 8 Fay's 12a Federal Express 23c Federal Natl. Mtg 17a Federal Paper Board 7b Federal Signal 15a Ferro 4 Fieldcrest Cannon 15d Figgie International 5 Fino 11b Fingerhut 8 First Bank System 3b First Chicago 3b First City Bancorp 3d First Fidelity 3a First Financial Mgmt. 17a First Interstate Bancorp 3d First Mississippi 4 First of America Bank 3b First Union 3c Fleet/Norstar 3a Fleetwood Ents 14d Fleming 10a Florida Progress 24a Florida Steel 16b Fluor 21a FMC 15c Food Lion 10c Foodarama 10c Ford Motor 2a Foster Wheeler 21a FPL Group 24a Freeport-McMoran 4 Fruit of the Loom 6a Fuller (H. B.) 4 Fuqua Industries 5	H Halliburton 11c Hanna (M. A.) 4 Hannaford Brothers 10c Harley-Davidson 14d Harnischfeger 15c Harper Group 23c Harsco 15a Hartford Steam 17b Hartmarx 6a Haskins 14d Hawaiian Electric 24a Hechinger 8 Heilig-Meyers 6b Heinz (H. 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C.) 8 Pennsylvania Power 24a Pennzoil 11b Pentair 15c Peoples Energy 24b Pep Boys 8 PepsiCo 6c Perkin-Elmer 9c Perry Drug Stores 12a Pet 10b Petrie Stores 8 Phizer 12b Phelps Dodge 16c PHM 23c Philadelphia Electric 24a Philip Morris 6c Phillips Petroleum 11b Phillips-Van Heusen 6a PHM 13b Pic 'N' Save 8 Piedmont Natural 24b Pier 1 Imports 6b Pilgrim's Pride 10b Pinkerton's 21e Pinnacle West 24a Pioneer Hi-Bred 10b Pitney Bowes 18a Pittston 11a Ply-Gem Industries 13a PNC Financial 3a Polaroid 14d Pope & Talbot 19a Portland General 24a Postlatch 19b Potomac Electric 24a PPG Industries 13a Precision Castparts 16c Premark International 5 Premier Industrial 21b Preston 23d Price 8 Primerica 17a Promus 14c Provident Life 17b PSI Resources 24a PS Co. of Colorado 24a PS Co. of New Mex. 24a Public Service Ent. 24a Puget Sound Power 24a	Q Quaker State 11b Qualex 16b	S Safeco 17b Safeguard Scientifics 18c Safety-Kleen 21e Safeway 10c Salomon 17a San Diego G&E 24a Santa Fe Pacific 23b Scana 24a SCE Corp 24a Schering-Plough 12b Schlumberger 11c Schulman (A.) 4 Schwab (Charles) 17a Scott Paper 19b Scripps (E. W.) 20b Seaboard 10b Seagate Technology 18b Sears, Roebuck 8 Seaway Food Town 10c Security Pacific 3d Service Corp. Intl. 21e Service Merchandise 8 Shaw Industries 15d Shawmut National 3a Sherwin-Williams 13a Shoney's 14a Sierra Pacific 24a Signet Banking 3c Silicon Graphics 18b Sizzler International 14a Smith (A. O.) 2b Smith International 11c Smith's Food & Drug 10c Smithfield Foods 10b Smucker (J. M.) 10b Snap-on Tools 15b Society 3a Sonata 24b Sonoco Products 7b Southdown 13a Southern 24a So. New Eng. 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Sciences 21 Vons 10c Vulcan Materials 13	W Waban 8 Wachovia 3c Wackenhut 21e Wal-Mart Stores 8 Walgreen 12a Wallace Computer 1 Wang Laboratories 12 Warner-Lambert 12 Washington Post 20 Washington Water 2 Waste Management 1 Weirton Steel 16b Weiss Markets 10c Wellman 4 Wells Fargo 3d Westinghouse Electr Westmar Intl. 12d Westvaco 19b Wetterlo 10a Weyerhaeuser 19a Wheelabrator Techns Wheeling-Pittsburgh Whirlpool 6b Whitman 5 Wicks 15d Wicor 24b Willamette Industrie Willcox & Gibbs 21 Williams 24b Wisconsin Energy 2 Witco 4 Woolworth 8 Worthington Inds. 1 WPL Holdings 24a Wrigley (Wm.) Jr. 10 Wyle Laboratories 2	XYZ Xerox 18b Yellow Freight 23d Zenith Electronics 6 Zenith National 17 Zurn Industries 21a

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MARTIN SORRELL'S WHIP HAS MADISON AVENUE WINCING

WPP is forcing the same tough changes on Ogilvy that it brought to JWT. Is austerity the answer?

J. Walter Thompson and Ogilvy & Mather share a common owner, Britain's WPP Group PLC, and it is turning out to be one demanding parent. WPP is saddled with \$600 million in debt after acquiring the agencies in 1987 and 1989, respectively. Although WPP restructured the debt in April, investors have forced down its New York-traded stock from 21 to 4 in the past year, and the company has been plagued by rumors of a coming cash crunch. Now, as an ad recession pummels profits, WPP is demanding that both shops cut costs. At Ogilvy, the strain has hurt morale and threatened some big accounts. Thompson has already cut costs to the bone, but the pressure is unrelenting. Here's how both shops are weathering the storm.

OGILVY: EXITING EXECS AND WORRIED CLIENTS

Gallows humor is the order of the day at Ogilvy & Mather Worldwide Inc. "Want to rent some space?" asks Graham Phillips, who is trying to unload four floors of his spacious new Manhattan headquarters. The excess acreage is costing Ogilvy \$4 million a year at a time when the agency's chairman can't even afford such hoary traditions as David Ogilvy's annual \$100-to-\$300 Christmas bonus to agency employees. "The pain is awful," sighs Phillips. "I look at myself every day in the mirror and say: 'Why me?'"

Coming from an adman, such a *cri de coeur* is shocking. Advertising people usually cling to the belief that any problem can be cured by a big account win or a splashy new ad campaign. At Ogilvy, however, few executives predict a quick fix. Client budget cuts have driven agency revenues down 5% to 10% in the first half of 1991 compared with the same period last year, according to industry analysts. And there are even more ominous clouds on the horizon. The agency may lose longtime client American Express Co., whose \$60 million account is one of its mainstays.

AmEx recently asked two rival agen-

cies to come up with new ideas to market its green card. That's a big blow to Ogilvy, whose "Membership has its privileges" campaign helped craft a gilt-edged image for American Express. Now, AmEx is under siege from bank cards and new credit-card purveyors such as American Telephone & Telegraph Co. And the company wonders if its image is out of tune with the sober 1990s.

In a way, Ogilvy's problems mirror those of its client. Two years ago, O&M was the class act of the business: Red carpeting lined its hallways, and its staffers enjoyed equally plush treatment. Then, in May, 1989, British financier Martin Sorrell plunked down \$860 million for the agency. Since then, Sorrell's WPP Group has imposed strict financial discipline, leading to staffing cuts of almost 10% at the once paternalistic agency. "We're coming to grips with the end of an old culture and the beginning of a new one," says Bill Hamilton, creative director of Ogilvy New York. **SORE POINT.** The recession has made the transition all the more painful. Virtually all of Ogilvy's clients—from Duracell to Joseph E. Seagram & Sons—have reduced their ad budgets. Eastern Air Lines—and its \$45 million account—disappeared altogether. What's more, the perception of turmoil at Ogilvy has prompted several clients to consider yanking their accounts. In February, Hamilton says he barely prevented Hardee's Food Systems Inc. from pulling its \$80 million account.

As Ogilvy has lurched from crisis to crisis, morale has plummeted. Several senior executives have departed in recent weeks, and one former employee says staffers spend much of their time trading rumors about who's going to walk out next. Ogilvy executives say

compensation has become a particular sore point. WPP's tight financial controls, they say, have prevented it from promising hefty long-term bonuses, such as stock options, to key staffers.

The most visible departure was Gordon S. Bowen, the top creative executive of the American Express account, who left last month to head the Coca-Cola account at McCann-Erickson Worldwide. Bowen's loss has jarred Ogilvy's big client: "Any time you lose a talented person on your account, that's a concern," says an AmEx spokeswoman. Sor-

CREATIVE HEAD HAMILTON AND PRESIDENT LAZARUS: RAISING MORALE IS KEY



OGILVY & MATHER

- ▶ 1990 worldwide billings: \$4.56 billion
- ▶ Current U.S. billings: \$1.6 billion (est.)
- ▶ Key account moves: Lost Eastern Air Lines (\$45 million); won Kraft General Foods' Maxwell House Coffees (\$80 million), Northwest Airlines shuttle (\$8 million); retained Hardee's (\$80 million); may lose American Express (\$60 million)

DATA: COMPANY REPORTS, ADVERTISING AGE, ADWEEK

WPP still pays out bonuses.

The agency also chafes at Sorrell's ambitious profit targets. He wants Ogilvy to achieve pretax operating margins of 12%. In 1990, Ogilvy's margin was 10%. That discrepancy led to protracted bickering over costs between Sorrell and Manning. "It's messy, and it's demoralizing to all the employees," says one former senior executive. Sorrell acknowledges that it will take time to reach his target use of the recession.

LIFT. To be sure, Ogilvy's malaise hasn't faded throughout its far-flung agency network. Revenue is off in the U.S., Britain, Brazil, and Australia, while Ogilvy's other foreign offices have fared strong. And the hip New York office lifted on July 23, when Northwest Airlines Inc. promised it the right to buy from Donald Trump.

To boost the office further, the agency recently named Rochelle Lazarus to head Ogilvy New York. Lazarus, who was Ogilvy's successful direct-marketing manager, wants to "restore self-confidence." Now, though, she'll spend most of her time trying to salvage the American Express account, which she worked on for 11 years. Lazarus must convince clients that Ogilvy can refashion its image. If she can pull that off, Ogilvy will better shape to refashion its own.

By Mark Landler in New York

FRAYING CARPETS AND FRAYED NERVES

J. Walter Thompson Co.'s executives sympathize with their embattled colleagues at Ogilvy, it's because they went through similar agony four years ago. Thompson's costs were bloated, clients were starting to leave, and staffers wondered whether they would ever regain its prestige. To top it off, Martin Sorrell swooped in and acquired the 127-year-old agency in Madison Avenue's first hostile takeover.

Now, as the recession batters Thompson, its managers are drawing on the hard lessons they learned while whipping their agency into shape after the acquisition. "What's important is that all of our key players have gone through something much heavier than the recession," declares James B. Pat-

terson, JWT's No. 1 creative executive. WPP's tight financial controls have already worked big changes on the agency's free-spending ways. Thompson's chairman used to command a dazzling view of an interior atrium from a plush office that staffers dubbed the "glass palace." Burton J. Manning, the current CEO, runs Thompson from a functional office, while employees talk about raising money to replace the agency's frayed beige carpeting.

BALANCING ACT. Despite all the economies, the agency is struggling as reduced spending by clients such as Bell Atlantic Corp. cuts into margins. Analysts estimate JWT's revenue dropped about 2% in the first half of 1991 compared with last year. Thompson's 1990 pretax profit margin of 10.1% fell short of WPP's goal of 11%.

Now, with most of the draconian cuts already made, Manning is balancing his austerity program with a need to keep up employee morale and maintain the quality of JWT's advertising. He acknowledges that's no mean feat: "In the



MANNING AND PATTERSON: PRESSURE FROM WPP IS AN OLD STORY TO THEM

J. WALTER THOMPSON

- ▶ 1990 worldwide billings: \$4.62 billion
- ▶ Current U.S. billings: \$1.9 billion (est.)
- ▶ Key account moves: Lost Twentieth Century-Fox Film (\$35 million) and Vons supermarkets (\$20 million); resigned Bally's Health & Tennis (\$60 million); won most of Northwest Airlines' account (\$80 million)

DATA: COMPANY REPORTS, ADVERTISING AGE, ADWEEK

agency business, there's a point after which cost-cutting damages the fabric." So he has cut accounting and legal staffs rather than the creative or account teams. These departments helped Manning pull off JWT's recovery after the takeover by luring new business and producing slick ads for clients such as Löwenbrau beer.

Thompson's work for clients such as Listerine remains strong. But its new-business efforts have mostly stalled. Worse, the agency's Los Angeles office has been hit by a devastating string of account losses (table), while its Chicago agency has been mired in a slump. Patterson says he was unhappy with the leadership at the office, which now has a new general manager and creative director. He says clients lost confidence in

Los Angeles after it resigned the Bally's Health & Tennis account when it couldn't agree on compensation.

That's why Thompson exulted last month when Northwest Airlines Inc. awarded it the bulk of its \$90 million account. Along with Ogilvy and two other agencies, Thompson will create a unified global campaign for Northwest. That means, for example, that Thompson could find itself producing commercials based on an Ogilvy strategy. Christopher Clouser, Northwest's advertising chief, says he discussed the unorthodox arrangement with Sorrell, who assured him that both shops could make it work.

TOP-HEAVY? Clouser also says he will pay close attention to changes in staffing at Thompson, which, like Ogilvy, has lost several executives in the past month. One industry headhunter says Thompson's staffers are frustrated by the agency's top-heavy management.

But Thompson isn't suffering the sort of talent drain that afflicts Ogilvy. Executives familiar with both say that's because Thompson isn't feeling quite as much budget pressure. They credit Manning's leadership and forceful style in negotiating profit targets with WPP. "The philosophy on their side is 'demand the outrageous,'" explains Manning. "On our side, it is 'give the least.'"

Manning's in-your-face style hasn't shielded JWT from the recession. But by learning how to maneuver inside a penurious holding company, he has persuaded Thompson's battle-scarred veterans that there is life after a takeover.

By Mark Landler in New York

WHAT HAPPENED TO THE AMERICAN DREAM?

THE UNDER-30 GENERATION MAY BE LOSING THE RACE FOR PROSPERITY

When Troy Marshall finished high school four years ago, he saw no point in trying to follow in the footsteps of his father, a lineman at a Cleveland electric utility. After all, such well-paid union work has become scarce in the past decade. Marshall worked as a travel agent before deciding, at age 22, that sales might be his ticket to the middle class.

With that move, Marshall, like much of his generation, has begun a desperately long climb toward the \$40,000-a-year lifestyle of his 44-year-old father. By day, Troy sells office supplies to small companies. By night, he cares for Cory, 3, and Cameron, 2, while his wife, Linda, 23, fills orders at a Cleveland Taco Bell. Together, the couple makes about \$20,000 a year—44% less, adjusted for inflation, than Troy's father alone earned at the same age. The elder Marshall owned a home by the age of 21, and his wife didn't work. The younger Marshalls, by comparison, lived with Troy's grandmother until recently and have no savings, much less the \$10,000 downpayment for a modest house in suburban Cleveland.

"My wife's parents keep telling us they had to struggle when they started out," says Troy. "They tell us things will get better. My goal is to catch up to the level of affluence my parents have. But it definitely won't happen overnight."

It may not happen at all. Since 1973, America's basic engine of prosperity—productivity, or output per worker—has grown at one-third the rate of the previous 25 years. When productivity lags, employers struggle to keep their costs in line, and in doing so hold down pay. This has happened especially in the part of the economy that has created most of America's new jobs over the past two decades—the service industries. In manufacturing, meanwhile, the traditional high-wage fortress of America, foreign competition erased millions of jobs in the 1980s, and employers clamped down on pay for the ones they kept. Older workers have been somewhat insulated, since their incomes reached comfortable levels before the malaise set in, or were high enough to let them borrow extravagantly. But the bucks have stopped at the group known as the "baby bust" generation—some 75 million people aged 10 to 30.

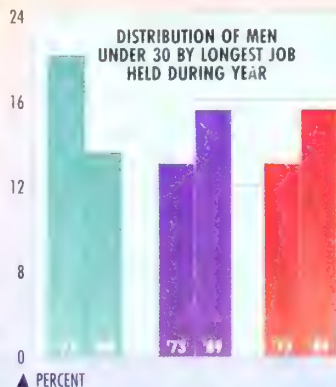
Obviously, not everyone in this group is suffering: doc-

tors, programmers, even a few investment bankers, continue to beat the averages. But the averages look just plain bad. Measured in inflation-adjusted dollars, the median income of families headed by someone under 30 is now 19% lower than such families earned in 1973, according to an analysis of Census Bureau statistics by Northeastern University's Center for Labor Market Studies. The best-off segment of this group, 14% of families headed by a college grad, would show a slight loss in real income, not a 16% gain, were it not for working wives. And from there on down the news is devastating. The real incomes of under-30 families headed by high school graduates have fallen 16%. For dropouts the decline has been a dizzying one-third, for blacks, the same, and for whites, 5%.

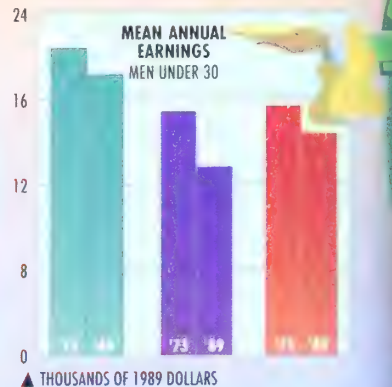
LOST OPPORTUNITIES. "Young families are in an economic free-fall despite the longest boom since World War II," declares Clifford M. Johnson, director of family support at the Children's Defense Fund in Washington. In fact, says Frank Levy, an economics professor at the University of Maryland, the baby bust generation may never match their parents' living standards. And that, says Jeffrey G. Williamson, an economic historian at

THE PLIGHT OF THE UNDER-30 GENERATION

MORE WORK IN SERVICES...



...WHERE PAY IS LOW...





Troy Marshall and his wife, Linda, both work, caring for sons Cameron and Cory in shifts. After adjusting for inflation, their income is about half what Troy's father earned in his 20s—while Troy's mother stayed home

Harvard University, would make them the first U.S. generation ever not to do so since the Great Depression didn't afford an entire generation.

With more than 30 years of earnings still ahead for these people, it's too early to write them off. After the recession, the labor shortages of the 1980s may reappear, forcing pay up. And the share of young families headed by college grads will increase, to 22%, once all the baby busters finish school. Still, even if the twentysomething generation ultimately does as well as its parents, it will do so at a much later age, predicts Andrew Sum, who heads the Northeastern labor center. The lag will be measured in opportunities lost: a longer wait for a home, more parents who must work in-

stead of care for their children, and a widening gap between rich and poor.

The fallout will touch more than just the young. Experts have long predicted that the baby bust's smaller numbers would give them better opportunities when they joined the work force than the overcrowded baby boom enjoyed. If the opposite continues to happen, generational conflict may occur. "Asking young people to lower their expectations is like telling someone to change the color of their eyes," says Douglas Coupland, 29, author of *Generation X*, a new novel that chronicles the cynicism of his age group. Champions of children already argue that a disproportionately small share of federal spending goes to the young (page 85).

Indeed, if busters must struggle to support their families, social programs may grow faster than the generation's thinner ranks suggest they should. Some busters may end up as depressed as their incomes, spawning a higher incidence of psychological and medical problems. Hardest hit may be children, whose poverty rate is up a third since 1973. "You're more likely to have chronic health problems if you grow up poor," says Marilyn Moon, health care expert at the Urban Institute. "And children with young parents tend to be poorest," she adds.

Beyond all

PHOTOGRAPH BY ROGER MASTROIANI CHART BY ROGER DOWNEY, EW

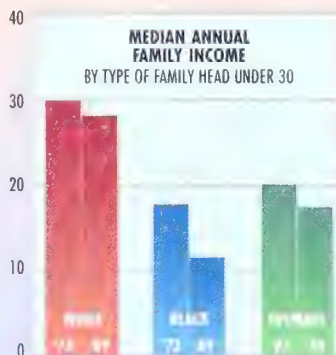
...SO INCOMES HAVE DROPPED...

MEDIAN ANNUAL FAMILY INCOME BY AGE OF FAMILY HEAD



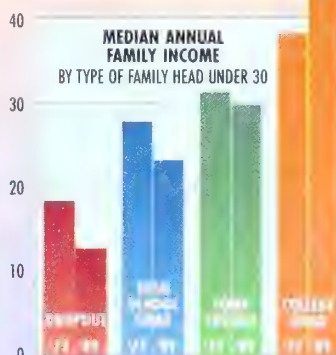
...DEVASTATING MINORITIES...

MEDIAN ANNUAL FAMILY INCOME BY TYPE OF FAMILY HEAD UNDER 30



...AND THE LESS EDUCATED

MEDIAN ANNUAL FAMILY INCOME BY TYPE OF FAMILY HEAD UNDER 30



DATA: NORTHEASTERN UNIVERSITY, CENTER FOR LABOR MARKET STUDIES





this every generation. The baby boomers put fewer dollars into circulation. For instance, homeownership among the youngest members of the baby boom—those aged 18 to 24—fell by more than seven points, to 54%, from 1980 to 1990. If boomers enter their 30s and 40s with reduced real incomes, they'll buy less, too: fewer houses, cars, and luxury goods of every variety.

That would end what for most Americans has been 50 years of pretty good times. The generation that started work after World War II was "the lucky one," Levy says, since it reaped the benefits of fat productivity gains—3% a year—in the 1950s and 1960s. Real wages rose so fast that male breadwinners could buy 30% more than their predecessors had a decade before. Even blue-collar workers could afford bigger houses, second cars, and college for their kids.

That generation has surpassed in income gains and net wealth every generation that preceded it—and, so far, all that have come after. In fact, it may represent the high point for U.S. living standards, considering that baby-boom families may surpass it only by having two wage earners. Because more than 75% of new jobs are in services, where productivity has barely budged in 30 years, few economists expect a quick re-

Curtis Smith works—but can't afford to live with his girlfriend.

Lawanda, and their children.

LaQuan and Brandy

turn to the robust productivity and real wage growth of the '50s and '60s. That period "was unprecedented and may never be duplicated," says Levy, the co-author of a new book called *The Economic Future of American Families*.

'McJOBS.' The most obvious cause of the baby boomers' plight is that male wage earners are landing worse-paying jobs. On average, young men today earn 17% less, in inflation-adjusted terms, than they did in 1973. For the most part, adding women to the work force hasn't offset the decline. Single mothers, who head 24% of young families, drag down the average income of young families. And in any case, working women make only about 65% of what men do. "Young families are working harder for less pay," says Heidi Hartmann, director of the Institute for Women's Policy Research in Washington. "And that doesn't

count the costs of having a second worker, like commuting expenses, work clothes, and child care."

The shakeout in manufacturing dealt one of the biggest blows. From 1973 to 1980 the proportion of 20- to 24-year-old men in the work force who toiled in factories fell to 25% from 30%. Because the last hired are usually the first fired, the share of men under 25 dropped twice as fast, to 19% from 28%. And pay has fallen for the few factory jobs that open up. Union concessions played a part, starting a decade ago. For instance, the rapid spread of two-tier wage scales, which pay new employees at a lower rate for the same job, hurt young workers most. Beyond that, as companies such as American Telephone & Telegraph Co. and the Ford Three auto companies have cut hundreds of thousands of hourly jobs, much of the remaining work has migrated toward smaller, nonunion shops that pay less and subcontract for the large companies. Overall, young men in manufacturing today earn 8% less in real terms than the counterparts did in 1973.

Faced with less opportunity in factories, the Troy Marshalls of the county have moved into industries that traditionally have hired women: services and retail sales. But these jobs pay 15%

less than men under 30 make in ries. And they pay even less than used to, adjusted for inflation. is also reflects subcontracting and tier pay scales. But another factor is id increase in the number of part- and temporary jobs in retail trade services. These pay 40% less per on average, than full-time work. the number of them has jumped y 20% since 1973, to a healthy—or althy, depending on your view— of the total. Until recently, more- Congress hasn't done any favors minimum-wage earners, 80% of a work in service jobs. Although minimum wage recently boost- o \$4.25 an hour, nguished at \$3.35 nearly 10 years. e's a debate over her a higher mini- prompts employ- to eliminate low- e jobs—and is erproductive. But e's no argument in real terms, the nt floor is 20% be- 979's. The bottom s that young men ervice jobs earn less in real terms 20 years ago. And sales jobs pay less.

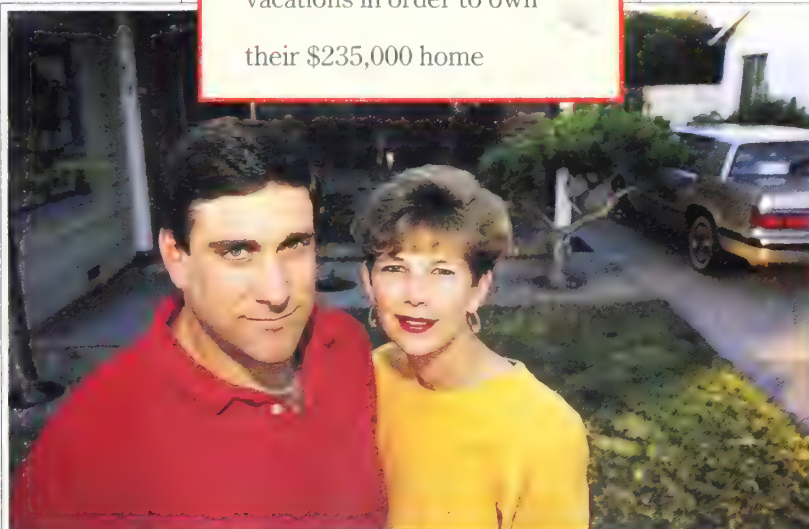
e people who end up in these obs," as Coupland calls them, also longer to land full-time positions. In a majority of high school dropouts found steady work by age 22, acing to Census Bureau data. Today, es until about age 26. While they're ng, young men go through more longer unemployment spells than counterparts 20 years ago. In any year, 1 in 10 males aged 18 to 29 s nothing—up 40% since 1973. Many hus stuck at home until well into twenties.

ADIC WORK. A case in point is Cur- . Smith Jr., 24, an 11th-grade drop- from Flint, Mich. He grew up plan- to be a unionized auto worker like ather, mother, and grandfather be- him. But as the industry shrank, ar companies stopped hiring, even ush times. So Smith gave up his s of an assembly-line future. In- l, he has worked as a fast-food a dishwasher, and in hotel mainte- e. Two years ago, he signed on with ntemporary agency that does contract : for nonunion auto-parts makers. last job he had as a temp, stamping s for a small metal-working compa- paid \$4.25 an hour and lasted a few hs. After that, he gave up on tem- rary work and became an asbestos re-

mover. Because that's hazardous, it pays \$9.26 an hour. But the work is sporadic: Smith works a maximum 20 hours a week, and some weeks hardly at all.

On an income of some \$9,000 a year, Smith can't support his girlfriend of five years, Lawanda Walker, and their two

College-educated Craig and Letia Hunter have sacrificed savings and vacations in order to own their \$235,000 home



children, LaQuan, 4, and Brandy, 2. So he lives at home, while Walker and the kids collect welfare and live with her mother a mile away. Smith dreams of getting his own place but feels that the risk is just too great right now. He wonders whether he will ever match his parents' lifestyle. "More people ain't coming to that level," he says. "It worries me, because I have two kids myself."

In fact, the proportion of children living in poor households has jumped more than five points since 1973, to nearly 20%, vs. the nation's 13% overall poverty rate. This translates into nearly 13 mil-

lion poor kids under 18, whose growing ranks have halted progress on improving child health. One barometer, the U.S. infant-mortality rate, dropped dramatically in every decade from the 1940s through the 1970s. But in the 1980s, it barely budged. The U.S. is now in 19th place in the world on this score, behind countries such as Singapore, Spain, and the former East Germany. The U.S. is No. 17 in the share of 1-year-olds who are immunized against polio and No. 28 in children who are born at the proper weight.

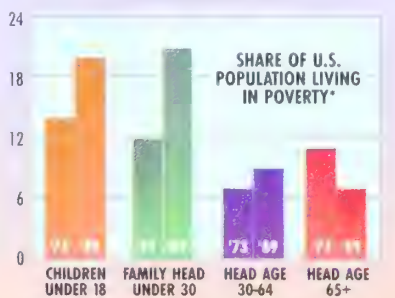
DOUBLE WHAMMY. Pick any of these problems, and under-30 minorities are the worst off. In part, this reflects the higher share of young black families headed by single mothers—58%, vs. 16% for whites. In part, it's because both blacks and Hispanics are less educated than whites and because they still face not-so-subtle job-market discrimination. In fact, the double whammy of more single mothers and lower male earnings has hit young black families as hard as the Depression hit nearly everyone in the 1930s. Their real medi-

an income is down an incredible 33% since 1973, to \$12,000 a year, according to Northeastern University's figures. Incomes of young Hispanic families, who have fewer single mothers, are down 13%.

Stanley and Olivia Glass are among the more fortunate young black couples. Stanley, 23, has had his share of modest jobs since he began working at 14: bus-boy, janitor, delivery-truck driver, and cook—the \$9,500-a-year job he currently holds with the Atlanta public schools. He is taking night classes at a community college, hoping to improve his earning power. And Olivia, 22, earns \$13,000 a year as a nursing aide.

But even on nearly \$23,000, the family feels pinched. With two kids, Crystal, 2, and newborn Stanley Jr., the Glasses rarely eat out and don't take vacations. Instead, they concentrate on the monthly bills: \$375 to rent a two-bedroom apartment, \$193 for car payments, \$182 for health insurance co-payments, \$232 for child care. A house of their own is a distant dream, and Olivia, whose father drove a city bus, longingly recalls life with her parents, who owned a ranch-style home, ate out often, and vacationed every year. "We weren't rich, but we weren't poor," she says. "We lived comfortably." By contrast, says Stanley,

MORE CHILDREN AND YOUNG FAMILIES LIVE IN POVERTY



DATA: NORTHEASTERN UNIVERSITY, CENTER FOR LABOR MARKET STUDIES, CHILDREN'S DEFENSE FUND

"things are very hard" for his family.

As baby busters of all races fall behind, two mainstays of middle-class life—homeownership and retirement security—are increasingly elusive. In the 1980s, rising prices and high real interest rates squeezed nearly everyone who didn't already own a home. But because busters came into the market later and earn less, more of them were priced out of the market. Recent price declines may help, but homeownership among house-

holds headed by people under 25 dropped from 23% in 1973 to under 18% last year, according to a recent study by Harvard University's Joint Center for Housing Studies. Among 25- to 29-year-olds, homeownership has fallen from 44% to 35%. Renting isn't a solution. With incomes down and rents up, rent as a share of the median income of young Americans has jumped by 50% since the early 1970s, according to the Harvard study. Today, under-25 households fork out 36% of their gross income on rent.

LESS PAIN. When busters start to contemplate old age, they fear that "the worst is yet to come," says Kathryn A. Lowell, 26, a congressional aide in Washington. Service industries and non-union companies typically offer fewer pension plans than the stalwarts of Industrial America. As the best factory jobs have disappeared, the share of men under 35 enrolled in company-financed pension plans has dropped from 46% in 1979 to 37% in 1988, according to the Social Security Administration. Adds Lowell: "When we get older, and the boomers have obliterated the Social Security funds, that's when we'll feel the real effect" of these trends.

The best protection from this may be a college degree, though, surprisingly, college-educated young men earn 2% less, in real terms, than in 1973. Working wives have offset the drop, accounting for the fat 16% income gain of such couples, adjusted for inflation.

The Hunters are a good example. Letitia, 28, is a salesperson for Bell & Howell Co. Her husband, Craig, who just turned 30, works as an accountant at Dataquest Inc., a high-tech market research firm in San Jose, Calif. The cou-

ple, who both have BAS from California State University at Stanislaus, will pull in about \$67,000 in 1991. Married just a year, the Hunters don't plan children for another two or three. That's why they could swing the \$235,000, three-bedroom bungalow they bought last December near downtown San Jose.

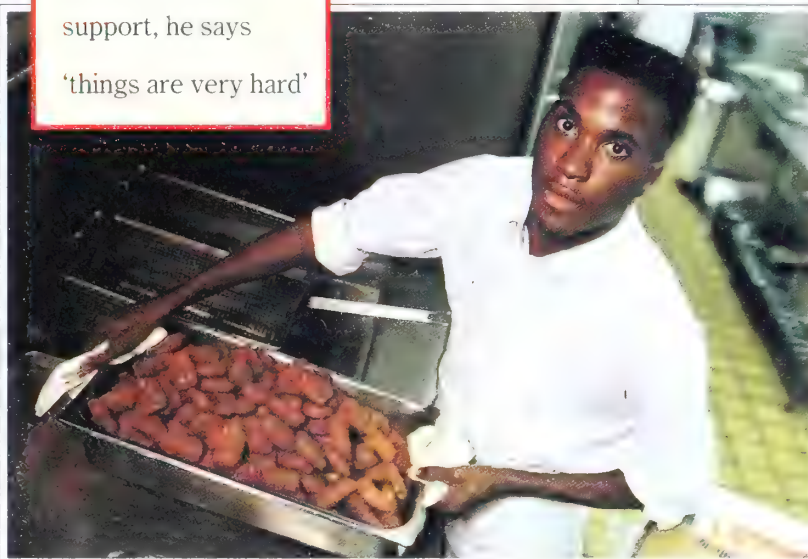
Still, the Hunters are behind in relative terms. "My parents were a single-income family with a new home, savings, and vacations," says Craig. He and

Letitia forgo savings and vacations to pay their mortgage. "We have two incomes and a 40-year-old home, and we're making it. But not as well as my parents did on one income," Craig adds.

The recession has made things worse for busters

Stanley Glass and his wife have jobs. But with two children to support, he says

'things are very hard'



of all educational levels. The economy shed 1.45 million jobs in the 12 months ending in March, and 16- to 24-year-olds accounted for nearly 65% of the decline, according to Northeastern University's Andrew Sum. Since this group constitutes only 17% of all workers, it has suffered roughly four times the pain of other age groups.

As usual, blacks and dropouts have been hardest hit. The employment-to-population ratio of 16- to 24-year-old dropouts fell by 2.7 percentage points over the past year, vs. a 1-point decline for people 25 and over, says Sum. The ratio for young blacks fell by five points. "Young blacks and dropouts made important gains in the last half of the 1980s, primarily because of labor shortages," says Sum. "Now, they've lost it all because of the recession."

The longer-term outlook for young Americans may not be entirely bleak. One potential bright spot is housing.

Some experts say the big price jump is over for a while, which eventually should let more busters buy homes. Then, too, the current pay premium for college degrees is a sharp reversal from the 1960s, when a glut of educated employees drove salaries down. Some labor economists believe the trend may flop again. Until the recession arrives, Sum notes, the real incomes of both men and dropouts rose, even though their hourly pay lagged inflation, so more hours of work were available.

Some analysts expect labor shortages to return after the recession and to last through much of the 1990s. If this happens, pay prospects may improve again for all busters, and especially for 60% of young workers who don't attend college. And, seeing the premium degree commands, busters may stay in school longer, further worsening

the shortage of less-skilled workers. "The education gap—between workers with college degrees and those without—is unusually large now," says Marvin H. Koster, economist at the American Enterprise Institute. "The question is how much impact counter-trends will have" in closing the gap.

Still, many economists argue that productivity holds the key to future earnings. And here, the prognosis may not be good. In his book, Levy projects

incomes for men who were 30 in 1969 against earnings of their fathers, who he assumed were 55 that year. In both of those scenarios, both involving employment of 5% and no trade deficit by 1992.

In the optimistic case, U.S. productivity grows at the historic norm of 1.9% a year. By 2006, a high school graduate would earn about \$30,000 a year in 1990 dollars—about what his similarly educated father made in 1966. But if productivity grows at 1.25% a year, as it did in the 1980s, the son's income will fall 20% below his father's in his peak earning years. Because of labor shortages, "the baby bust might do better than other cohorts in the next 5 or 10 years," says Levy. "But that will be more than offset if productivity grows slowly."

Unfortunately, even brisk productivity growth no longer guarantees rising wages. Factory efficiency rose 40% in the '80s. But part of the gain came from

very trends that hurt young work-such as part-time and subcontracted. These may not diminish. A recent Federal Accounting Office report says that such "nontraditional employment" should maintain or expand its share of the work force in the 1990s." But if the earnings of men don't rise, it's only one way young families will suffer: Wives must work more. That can happen. But there's a limit. Anyway, couples under 30 have 1.79 earn-

ers on average, up from 1.67 in 1973, according to Sum. Young families put in 3,340 hours of work a year. Since a full-time job usually involves about 2,000 annual hours of work, these families could, in theory, work 20% more. However, women still might not make enough to overcome the decline in real incomes if the wages of men slide further. "As wives get older, they should earn more," says Sum. "The question is whether this will be enough to make up the

13% drop in young families' incomes." It is no doubt premature to condemn the baby-bust generation to permanently lower living standards. But it seems increasingly likely that America's young people are going to mature in a less affluent world. And that spells trouble for all Americans, young and old alike.

By Aaron Bernstein in New York, with David Woodruff in Detroit, Barbara Buell in San Jose, Nancy Peacock in Cleveland, and Karen Thurston in Atlanta

IS UNCLE SAM SHORTCHANGING YOUNG AMERICANS?

Until recently, hardly anyone analyzed government spending in terms of age. But the more extensive look, the larger the inequities seem. Some 29% of federal outlays go to people 65 and older, according to the Congressional Budget Office (CBO), while children under 18 get 7%. Even after allowing for the \$200 billion a year in local public school funding, the U.S. spent \$4,500 per child in 1990—\$11,300 each on 31-year-olds. This hasn't happened entirely by design. In 1965, the elderly got just 16% of federal outlays, the CBO says. Then, after Congress indexed Social Security benefits to the cost of living in the 1970s, double-digit inflation drove the tab up through the roof. And in the 1980s, Medicare costs surged as medical inflation soared.

OLDER KIDS. Still, there has been some criticism at budgeting time. "In many cases, Congress has consciously cut programs for children more than those serving the elderly," says Robert Greenstein, director of the Center for Budget & Policy Priorities, a liberal research group in Washington. A case in point is welfare, 29% of whose recipients are children and men under 30.

Grants for these people have fallen 40% behind inflation since 1970. And thanks to tightened eligibility, 58% of poor children receive welfare now, vs. 81% in 1973. The result is a discrepancy in who is getting lifted out of poverty. The child poverty rate—the share of

all children living in poor households—has jumped to nearly 20%, from 14.4% in 1973. Meantime, the poverty rate for the elderly has fallen, to 6.6% from 10.5%.

Young adults have lost out, too. It is well-documented that unemployment insurance covers a smaller share of jobless workers now than a decade ago. Mostly to blame are trends that reduce the ranks of eligible recipients, such as increased part-time work. Much of the burden falls on workers under 35—the group with the most part-timers. Only 18% of jobless workers this age collected unemployment in 1990, vs. 38% in 1979.

Now, pressure is rising to redress many of these imbalances. In June, the National Commission on Children, which Congress appointed in 1987, recommended a \$1,000-per-child income-tax credit to help families with kids. It also wants mandated health coverage—supplied either by employers or the government—for

the 8.3 million children and 430,000 pregnant women who annually lack medical insurance. The commission, headed by Senator John D. Rockefeller IV (D-W. Va.), pegged the cost of all this at up to \$56 billion a year.

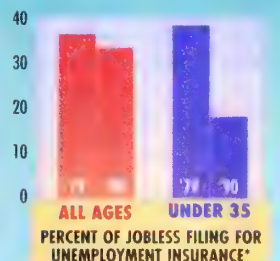
The options the commission pointed out include raising taxes or cutting spending on military or space programs. Even advocates for children are cautious about another obvious source: reserving Social Security for those who need it most. That would leave more for the poor. But if Social Security becomes just another poverty program, "the middle class would have no stake in it, which could be a recipe for political disaster," says Clifford Johnson, director of family support at the Children's Defense Fund.

SOAK THE SENIORS? A wiser idea politically may be to raise the tax on Social Security benefits. Two years ago, a Ford Foundation report suggested taxing benefits that exceed an individual's lifetime contribution. This would raise more than \$25 billion a year. Even groups such as the American Association of Retired Persons don't rule out the idea. John Rother, AARP's legislative director, says it might go along to help children. "But only as part of an approach that involves contributions from everyone in society," he adds. "It can't be the responsibility of just one group, like seniors, who make up only 13% of the population."

Other sources of money could be more difficult to tap. Medicare has been reined in so much, for instance, that big new savings might involve health care rationing. "Maybe we will be forced to decide whether to give an extra dollar to better elderly health care or to a child to eat," says CBO analyst Paul Cullinan. Almost certainly not. But as the plight of young Americans becomes clearer, Congress may find that picking winners and losers among competing age groups will be an increasingly cutthroat business.

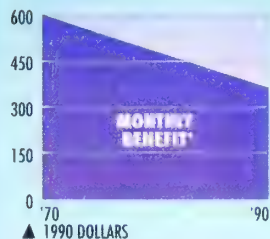
By Aaron Bernstein in New York

THE YOUNG COLLECT LESS UNEMPLOYMENT...



*Based on surveys in August of each year
DATA: LABOR DEPT., BUREAU OF LABOR STATISTICS

...ARE HURT MOST BY WELFARE CUTS...



*Maximum for three-person family in the median state. As of 1988, 85% of all recipients, including children, were under age 30

...AND GET LESS OF THE OVERALL FEDERAL PIE

	AGE 65 AND OLDER	UNDER AGE 18
TOTAL FEDERAL SPENDING* PER AGE GROUP	\$356 BILLION	\$85 BILLION
PERCENT OF TOTAL FEDERAL SPENDING	29%	7%
PERCENT OF U.S. POPULATION	13%	26%

*Fiscal 1990. Includes child nutrition, education, federal civilian pensions, food stamps, Head Start, housing assistance, Medicaid, Medicare, Social Security, unemployment compensation, welfare and miscellaneous

DATA: CONGRESSIONAL BUDGET OFFICE



CHAIRMAN HIGURASHI AND THE SVX: NISSAN WILL HELP OUT ON FUTURE MODELS

SUBARU PULLS INTO THE IMAGE SHOP

It's revitalizing its line of compacts and launching a sports coupe

Inexpensive. And built to stay that way." For years, that slogan summed up the appeal of a Subaru. As the U.S. marketing arm of Japanese auto maker Fuji Heavy Industries Ltd., Subaru of America Inc. prospered by selling four-wheel-drive compacts such as the GL for a modest \$6,500. But when the yen started to soar against the dollar during the mid-1980s, a Subaru was no longer such a bargain. Market share slipped. And Subaru responded by offering rebates of up to \$2,000 per vehicle—a move that resulted in a loss of \$130

million from 1987 to 1989. Suddenly, it seemed, Subaru wasn't built to stay.

But now, thanks to the clubby ways of Japanese corporations, Subaru is in the shop for a big repair job. Realizing that its pipeline into the U.S. was in danger of being choked off, Fuji last August shelled out \$66 million to acquire from the public the 50.4% of Subaru that it didn't already own. Another corporate sugar daddy, Nissan Motor Co., has also offered to help bail out Fuji and Subaru. Why Nissan? It's one of Fuji's largest shareholders and a fellow member of

the Industrial Bank of Japan Ltd. *Keiretsu*, a gaggle of companies bound together by interlocking shareholdings.

Together, Fuji and Nissan are looking to recast Subaru's image. In July, Fuji fired Levine, Huntley, Subaru's agency of 15 years, and awarded its \$4 million account to Wieden & Kennedy Inc., a Portland (Ore.) shop that has won critical praise for its hip Nike ads. It shore up the company's relations with consumers, Fuji is sending Subaru's 7,000 plus dealers and some 2,000 employees through special seminars on customer service. And back in Japan, Fuji is gaining plenty of manufacturing know-how from Nissan: Both are studying ways to save money through joint production, research, and transportation projects.

SPACE-AGE DESIGN. Subaru has already managed to halt its three-year market share slide. During the first half of 1990, Subaru's piece of the U.S. passenger car market edged up to 1.3%, from 1.1% at the end of 1990. That's still well below the 1.7% share it posted in 1987, but gaining new customers during a recession was no cakewalk. Subaru also hopes that its image will get a boost to fall with the roll-out of the SVX, a \$25,000 sports coupe with a powerful six-cylinder engine and a distinctive space-age window design. Says Takeshi Higurashi, a Fuji managing director who assumed the title of chairman and chief executive officer at Subaru of America in July: "Top [Fuji] management is very active in the American business."

Fuji management also has plenty of troubles to worry about back home in Japan. Its high production costs and reliance on low-margin minicars such as the Justy—also sold in the U.S.—have hurt the auto maker. Fuji's market share in Japan slipped from 5.5% in 1985 to 4.1% in 1990. In its fiscal year that ended Mar. 31, Fuji lost \$472.3 million on an unconsolidated basis.

Nissan, which holds a 4.2% stake in Fuji, has clearly been worried by the slide. Last summer, Nissan installed Isamu Kawai, who had turned around his company's money-losing truck business, as Fuji's president. Back in the

SUBARU'S U.S. OVERHAUL

TIGHTER MANAGEMENT

Parent Fuji Heavy Industries, asserting greater control, brought in its own executive, Takeshi Higurashi, as Subaru's new chief. To slash overhead, company has eliminated 11% of its U.S. work force

FRESH MARKETING

Recently awarded its \$70 million account to Wieden & Kennedy, a hot Portland ad agency. The aim: Create a new image for Subaru's cars so they stand out from the pack of rival Asian nameplates

NEW PRODUCT

Subaru's SVX coupe due out this fall will add some sizzle to the carmaker's lineup of four-wheel-drive compacts. Expected to sell for about \$25,000, the SVX features a powerful six-cylinder engine

DATA BW

1970s, Nissan helped launch Fuji's into larger autos, and their ties since grown. Fuji recently agreed to resemble Nissan's Pulsar model at its just north of Tokyo, where it has y of excess capacity.

return, Fuji will pick up some cash manufacturing expertise from Nis- The two are also studying ways to a manufacturing efficiencies by de- ag parts that can be used inter- geably in Nissan and Fuji models. to save money, Nissan ships will transport Fuji cars to Europe.

of this helps. But Fuji's real aim is to recharge Subaru's sales in the its largest export market. When u enjoyed a big pricing edge, it y sold anything Fuji sent over. The days are long gone. Although it among the first to come out with wheel-drive passenger cars during mid-1970s, that market is now jam- ed with rivals.

TE WITHDRAWAL. Nowadays, Fuji tives are making their presence t Subaru—and how. Subaru recent- d off 110 employees, or about 11% f U. S. work force, saving about \$20 n a year. The survivors now attend iars by car consultant J. D. Power sociates Inc. on the importance of mer service. Subaru once ranked in J. D. Power's consumer satisfac- survey; it's now No. 11. Says Higur- "It's important for us to regain a ation for consumer satisfaction."

Subaru wants to regain its identity as rveyor of durable, practical cars. Wieden & Kennedy is preparing an mpaign that will position Subaru's cy and Loyale models as practical natives for individuals who don't v the herd—though it's unclear how h VX coupe, priced at \$25,000, will fit that strategy.

Subaru also hopes to reduce its addiction bates. Instead of offering cash, Su- has thrown in options such as air- tioning at no charge—a move that ouble the sales of its Loyale sub- act model this year. But Subaru discounts a fair bit. And its core cy model now faces stiff competi- from the Toyota Camry, among oth- ers. Says George E. Borst, vice-president strategic and product planning at ta Motor Sales USA Inc.: "Subaru's tough road ahead. Their buyer has more options available with four- l-drive vehicles."

ae enough. But things may be look- p. Subaru executives are predicting 1% jump in sales this year. And i the fraternal world of Japanese aking, it's unlikely the safety net be yanked out from underneath Su- and Fuji anytime soon.

James B. Treece in Cherry Hill, N. J., Karen Lowry Miller in Tokyo

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BATTEN DOWN THE HATCHES AND REV UP THE JACUZZIS

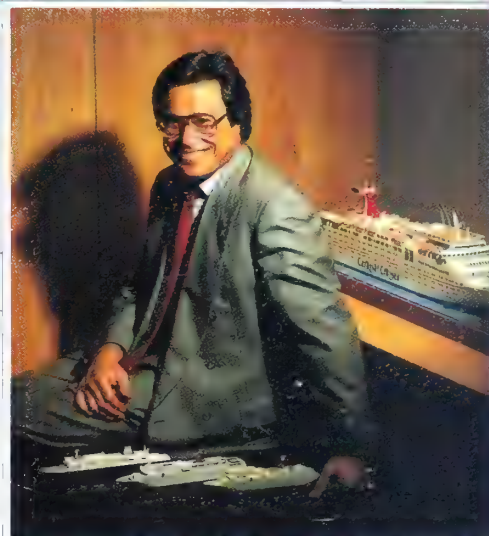
Carnival is prowling for more cruise lines to buy

Seas haven't exactly been calm lately for cruise-ship operators. Earlier this year, the gulf war jangled the nerves of travelers, deep-sixing cruise bookings. Nor did the recent recession leave folks with the wherewithal to whoop it up on the high seas. Now, cruise ship operators are fighting a bruising discounting war. And the industry's image took a plunge when a Greek liner, the *Oceanos*, sank off South Africa on Aug. 4. How is it, then, that the industry's lord of the seas, Carnival Cruise Lines Inc., continues to sail blissfully along?

By cruising with a young crowd, for one thing. Carnival Chief Executive and Chairman Micky Arison, 42, has successfully tapped into 25- to 39-year-olds—a

demographic group once given short shrift by cruise lines. The typical \$2,000-plus, two-week cruise has long been marketed to well-heeled middle-aged and elderly couples. But Arison has used a clutch of quickie package deals—such as a three-day, \$399 trip—to win over new and younger vacationers. Now, he's eager to build up the company's fleet, which sails under the Carnival, Holland America, and Windstar names.

The Miami-based line's success lies, in great part, in savvy marketing. It has been unusually skillful in overcoming cruising's image as a seagoing slumber party for the shuffleboard set. "Even in good times, the industry has not done a



MICKY ARISON: THE GULF CRISIS CAUSED NARY A RIF

good job in consumer awareness," says Robert Mahmarian, executive vice president at rival Costa Cruise Line. "Carnival is one of the exceptions."

Carnival has certainly brought some pizzazz to the business. Its advertising campaign features the perky cabaret singer and talk-show host Kathie Gifford prancing about the discos



lecks of a Carnival steamer. And its ships, with splashy names such as Easy and Ecstasy, boast neon lights, indoor whirlpools under skylights. Arison will use Carnival's clout to extend its industry's lead. Since the line's founding in 1972 by Micky's father, who retired as chairman last year—it has steamed ahead. Carnival now enjoys a 26% share of passengers in the \$5 billion cruise-ship market (chart). Later this year, the Arison family—which owns 82% of the company—hopes to raise \$218 million in a 7.85 million share offering that will be used mostly for acquisitions and debt repayment.

KEY IDEA. Carnival almost pulled off a nifty deal in April with its \$372 million bid for Premier Cruise Lines, a Cape Canaveral (Fla.)-based line that operates off Central Florida and has an exclusive marketing deal with Walt Disney Co. Premier's appeal to young families attracted Carnival, but the deal collapsed after both sides squabbled about price. Even so, Carnival has hardly lost momentum. Its passenger count has increased 20% during the first six months of the fiscal year, ended May 31. Carnival's average occupancy level is an astounding 103%—achieved by fitting

more than two people in a cabin—vs. the industry's 90% average. Investors are pleased: After dipping to a low of 11% last October during the Gulf tensions, Carnival's stock is now back at the mid-20s level it was trading at earlier.

Which isn't to say that Arison hasn't



hit a reef or two. Back in 1989, Carnival built the sprawling 1,550-room Crystal Palace Hotel & Casino in Nassau, Bahamas. The \$250 million fuchsia- and lavender-colored resort has been hit hard by a 20% downturn in Bahamian tourism. It lost \$21 million last year and will probably lose another \$10 million this year, figures Arison, who has said he may

sell the resort once it breaks even.

And while Carnival has kept its passenger count growing, its reliance on discounts—such as 2-for-1 deals on its \$519, four-day cruises—has been costly. Although sales were up 10%, to \$673.9 million, during the first half of 1991, profits fell 7%, to \$73.9 million. For the year, Carnival should turn in earnings of \$213 million, up 3%, on revenues of \$1.5 billion—a 15% improvement. Also, its spending spree on new ships—by 1994, it will add four to its fleet, for a total of 20—has boosted long-term debt to \$1.1 billion, or 50% of total capital.

Because of the upcoming stock offering, Arison isn't talking, but analysts don't rule out another run at Premier. Buying cruise lines is a thrifty alternative to paying about \$300 million to build a ship from scratch. Arison also has a shrewd eye: His 1988 acquisition of Holland America Line Inc. looks like a winner.

Meanwhile, the industry outlook will likely brighten in coming years. Passenger counts should increase by 10% or so a year, while capacity growth eases. Come the upturn, Arison may be able to extend his lead in the cruise business, leaving rivals floundering in its wake.

By Antonio N. Fins in Miami

ALBERTO MENA/FW

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FAST TALK, FAT CIGARS, AND BIG DEALS—IN THE '90s

Henry Silverman hasn't changed. He even wants Days Inns back

On one side of his office overlooking Park Avenue is something Henry R. Silverman likes to call his "wall of shame." In fact, it looks more like a wall of pride. Eschewing the austere decor favored by many banker types, the Blackstone Group LP general partner has adorned his wall with a hodgepodge of mementos: tombstone ads, press clips, baby pictures, and even a framed collection of his favorite witticisms in giant type. Among them: "Time wounds all deals" and "Let's rob the train before we split up the loot."

That sounds like 1980s talk. But then, Silverman is an '80s sort of guy. Unbowed by '90s protocol, in which humility is supposedly in and greed out, he presses on. The former head of a Saul P. Steinberg buyout fund, he still puffs Cuban cigars and drives a Bentley—only he is now at Blackstone, an investment boutique headed by former Commerce Secretary Peter Peterson.

Silverman, 51, was brought in early last year and is now coordinating the firm's LBO activities. Tapping the group's \$850 million equity fund, he bought the Ramada and Howard Johnson hotel chains last year for \$200 million. This year, say several people familiar with the deal, his fund is teaming up with Time Warner Inc. to buy the 80% of Six Flags amusement parks Time Warner doesn't own. Silverman won't comment on that purchase.

HOT POTATO. The deal that excites most curiosity, though, is Silverman's proposed purchase of Days Inns Inc.'s key assets. He has bought and sold parts of the hotel chain twice already (table) and is considered by some to be partly responsible for the unwieldy financial structure that may soon force a new sale. He first bought Days Inns in 1984, when running Reliance Capital Group. He took it public in 1986, private again in 1988,

and in 1989 sold it to Days Inns' largest franchisee—Tollman-Hundley Lodging Corp. The sale netted \$125 million—nearly a 400% gain for the original investors, Silverman says.

Silverman's original LBO was highly leveraged, and Stanley S. Tollman and Monty D. Hundley bought the company hoping they could restructure the debt before big payments came due. That proved impossible, and Tollman-Hundley defaulted on some bond payments in late 1990. Ever since, they have been wrangling with bondholders. Now, Silverman shows up, offering \$225 million to buy Days Inns' franchising agreements and reservations system—its crown jewels. The property would join Ramada and Howard Johnson in Silverman's Hospitality Franchise Systems.

Many Days Inns franchisees appear relieved by the idea, since it would mean more secure financial footing. But some bondholders are wary. One person close to the transaction calls Silverman's offer ironic, considering that he is "figuratively, the guy who brought them Pea Harbor." Tollman has also been heard to blame Silverman, but the dealmaker says he recently told Tollman: "Those guys were not naive babes. Don't tell me you didn't know what the debt was." Tollman and Hundley didn't return calls.

HAPPY WARRIOR. Smooth, articulate, and hard to ruffle, Silverman is respected as a dealmaker. But though he transformed the sleepy Southeastern chain into the nation's third-largest, some in the lodging industry still see him as an outsider, a Wall Street wizard whose deal-heavy transactions put Days Inns in a precarious position. "He has got a silver tongue," says one industry executive.

Silverman himself is filled with cocky self-confidence. He is fond of describing dealmaking as "like going to war, without the bloodshed" and clearly relishes the power. "You say 'jump,'" he says, "and legions of lawyers and bankers and investment bankers and accountants and consultants and PR guys and everybody else sort of jumps."

HE OWNS IT, HE OWNS IT NOT...

SEPT. 1984

Henry Silverman, head of Reliance Capital Group, buys Days Inns in leveraged buyout for \$570 million

JAN. 1986

Hotel chain goes public

JUNE 1988

Silverman takes Days Inns private again

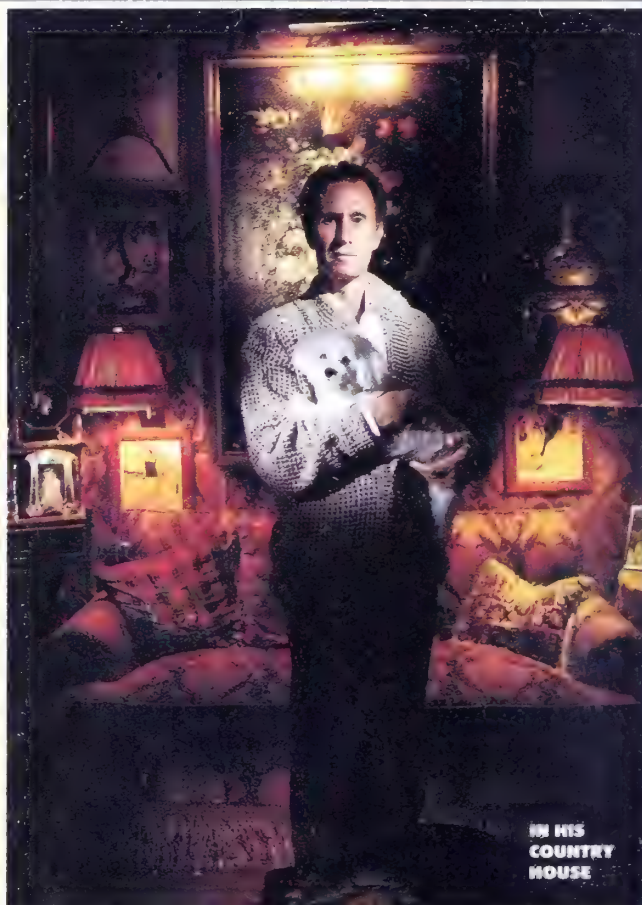
AUG. 1989

Tollman-Hundley Lodging buys Days Inns for \$765 million. Profit to original investors: \$125 million

JULY 1991

Now at Blackstone Group, Silverman offers Tollman-Hundley \$225 million for key Days Inns assets

DATA BW



's never short on boasts. His Park
ue apartment once belonged to
er Chrysler, he says. His country
e in Bedford Hills, N. Y., makes him
ighbor of Carl C. Icahn. His Cuban
ch Punch" cigars are so rare that
ears they could only be procured by
banese arms merchant friend, who
edly got them through the Cuban
nse Minister. Silverman smokes one
y, the seven-inch stogie protruding
his youthful face to give him a
cal look.

ming from a family of lawyers and
essmen, Silverman says he always
he would go into business. The
chester County (N. Y.) native got a
egree at the University of Pennsyl-
a, but practiced just a short time. He
t the next 15-odd years as a profes-
l investor and dealmaker and also
ed for various Wall Street firms.

1982, Steinberg invited Silverman
me to Reliance and set up an invest-
fund. Starting with \$60 million, Sil-
an invested in a flurry of medium-
deals, buying radio and TV stations,
'oo-Hoo chocolate beverage compa-
and John Blair & Co., which he
ed into the Spanish-language televi-
network Telemundo Group Inc.

LL SLOG. The deal that gave Silver-
the biggest stage was Days Inns.
the idea that the best advertise-
for a Days Inn is another Days
Silverman as chief executive put to-
er a high-powered sales force to per-
e hotel owners to convert to Days

He also marketed the economy
aggressively through a large res-
tions system, TV ads, and discount
el clubs." Silverman's record as an
ellent operating manager" made
a good catch for Blackstone, says
Stephen Schwarzman.

t Silverman will face a tougher cli-
if he gets Days Inns again. The
sion has put a damper on travel,
the chain has grown so large that
ough to add new units without cut-
into the business of existing fran-
s. Also, another company could still
up buying Days Inns.

verman has plenty else to keep him
. He has already added 200 hotels to
00 Ramadas and Howard Johnsons
ought last May, and he is pushing
urther growth. With roughly \$450
n left in the Blackstone fund, Sil-
an says he's interested in buying
-TV properties, which he says have
"upside" in pay-per-view and ad
ues. But he'll consider any good
any with too much debt. "We're
ng for businesses that are overle-
ged but haven't lost their franchise
he says. That sounds a lot like
Inns, coming from someone who
ld know.

By Andrea Rothman in New York

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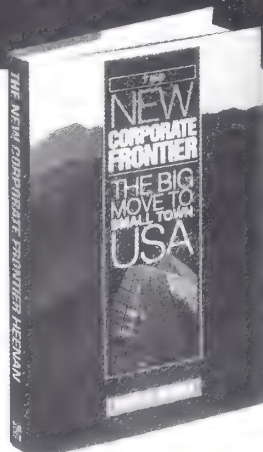
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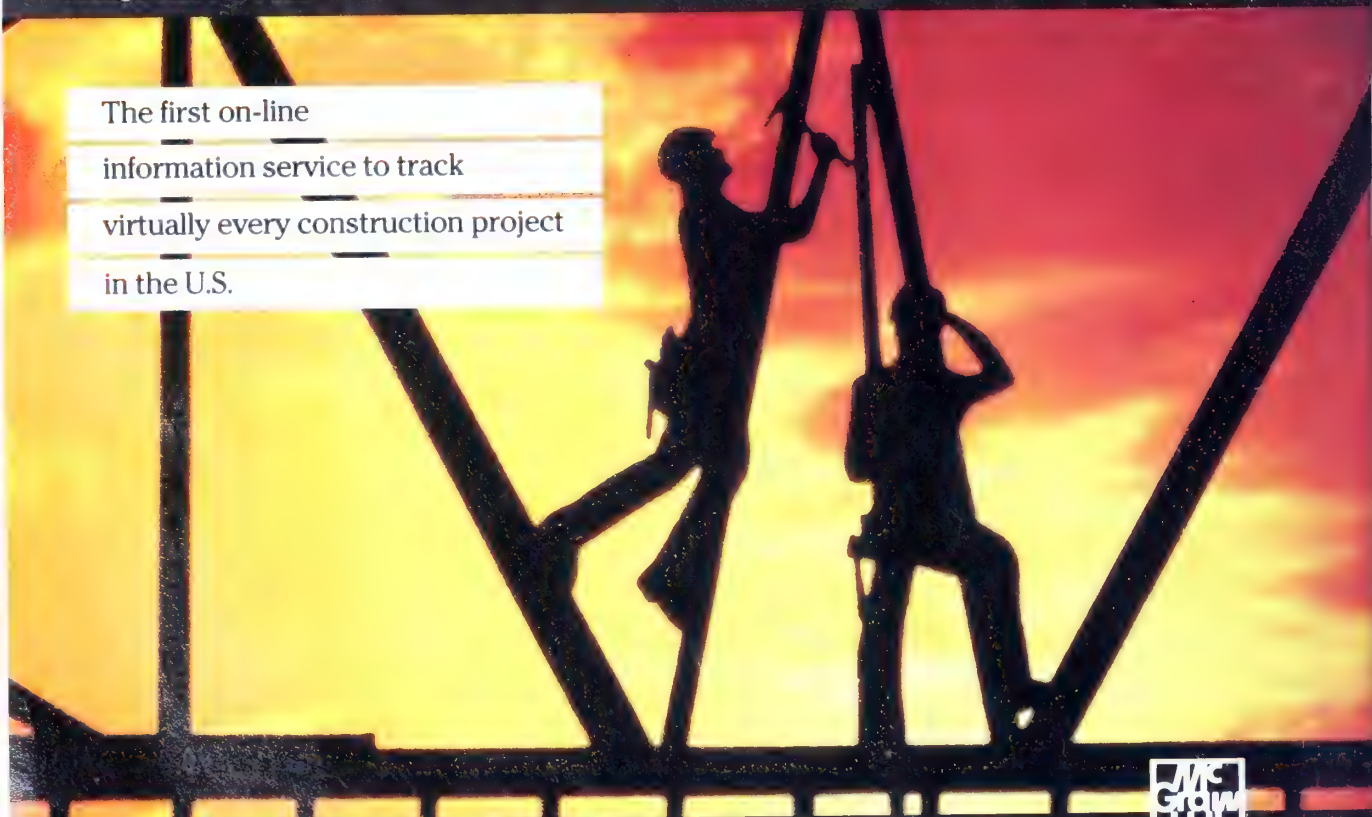
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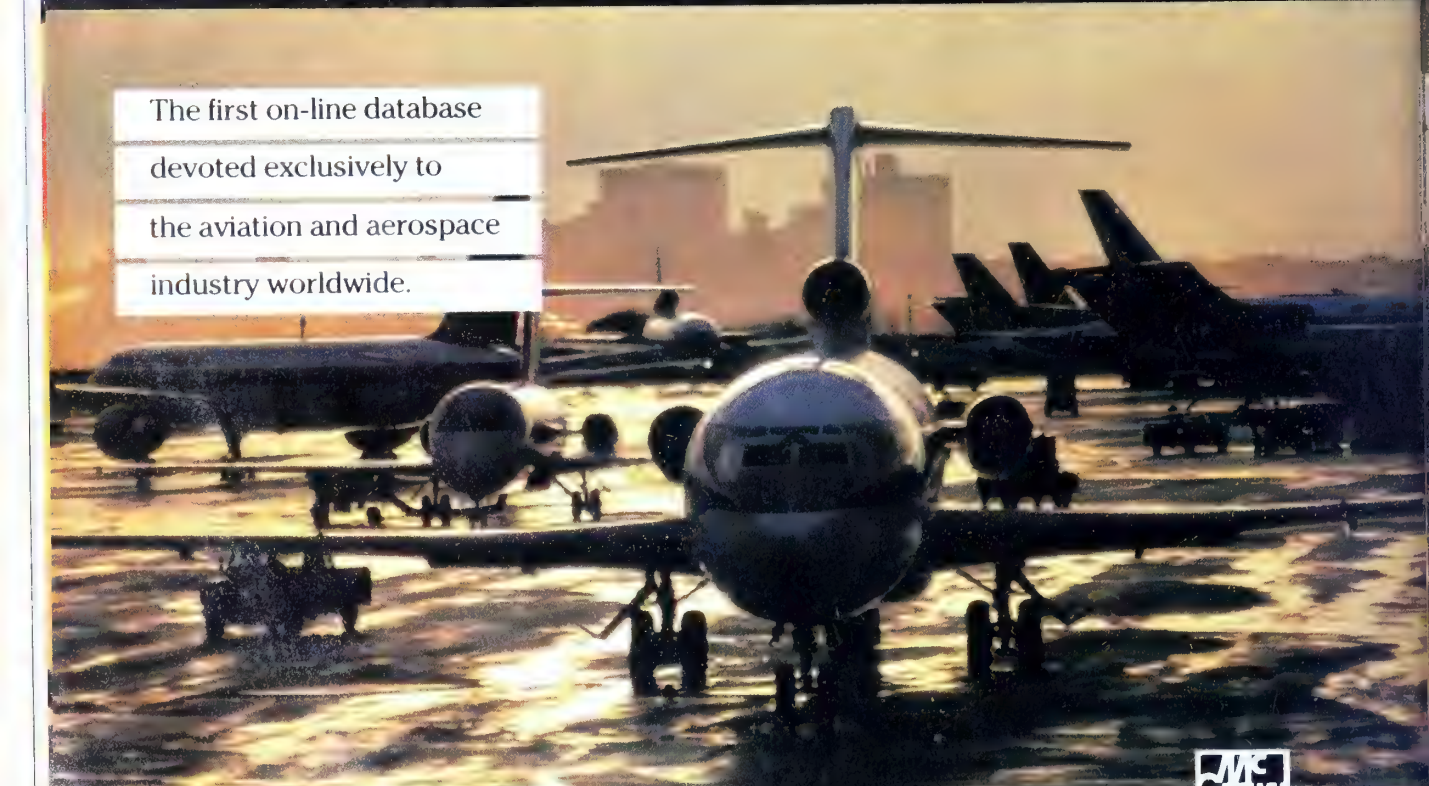


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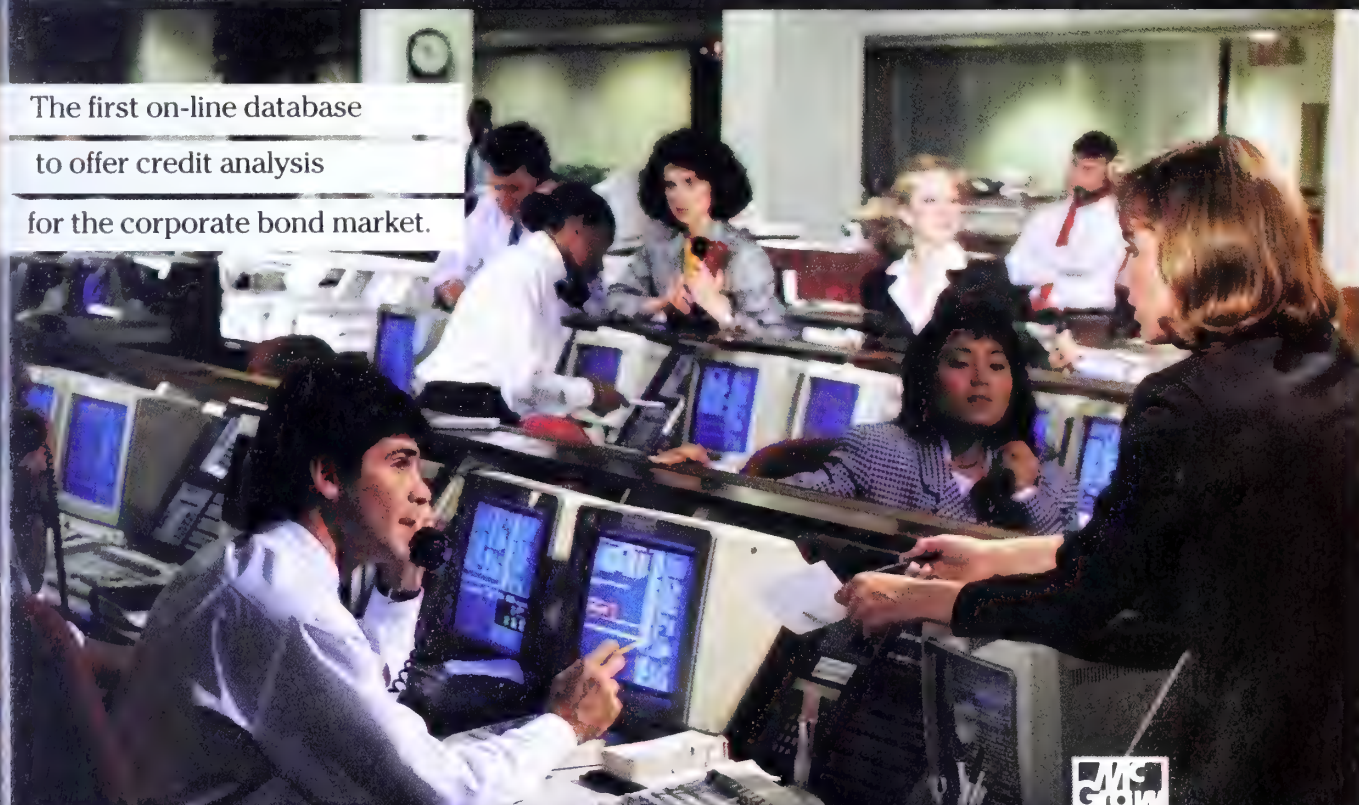
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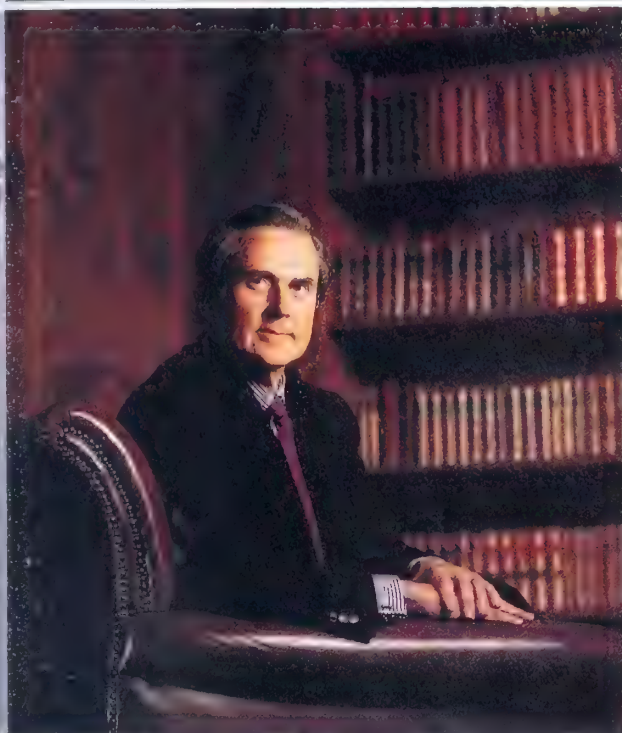
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CEO ROBINSON AND INVESTOR BUFFETT: THE FINANCIER SHELLED OUT \$300 MILLION FOR A PRIVATE ISSUE OF AMEX CONVERTIBLE PREFERRED

WHY AMEX WOODED WARREN BUFFETT

selling equity and assets to build up its balance sheet

During an American Express Co. finance committee meeting in mid-July, James D. Robinson III, AmEx's chairman and chief executive, was talking with John J. "Jack" Byrne, a fellow board member and head of American Cos., formerly Fireman's Fund Insurance Co. The two were talking about a topic much on Robinson's mind: his plan to raise equity for the credit-card giant. Suddenly Byrne had a storm. What about calling his close friend Warren E. Buffett? Byrne knew from his days running Geico Corp., an early Buffett investment. Robinson thought the O.K. Recalls Buffett: "I told him that I would be interested, and he said, 'Jim Robinson call me.'" Barely a week later, Buffett shelled out \$300 million for a private issue of AmEx convertible preferred stock.

During the imprimatur of the legendary Omaha investor was a great imprimatur for AmEx. Buffett's name con-

figures up images of brilliant investments in unbeatable franchises such as Coca-Cola Co. and Washington Post Co.

Yet AmEx needed Buffett's money much more than his name. Until recently, the company's financial strength was unassailable. Now AmEx is engaged in a far-ranging campaign to bolster its capital base. The main reason: continuing write-offs at its ailing brokerage unit, Shearson Lehman Brothers Inc. AmEx is feeling the strain of Shearson's balance sheet, which is very thinly capitalized. The broker's tangible net worth is on the rise, but at \$627 million, quite skimpy compared with its assets of \$66.5 billion. Further, AmEx has helped fund Shearson's problems with earnings from its once-robust card division, and those earnings are now slowing.

Despite Robinson's efforts to improve AmEx's capital position, Standard & Poor's Corp. in July downgraded AmEx senior debt from AA to AA-, almost cer-

tainly an embarrassment for the proud chairman. Now analysts suggest that AmEx is moving aggressively to avoid a further downgrade. Robinson acknowledges that rating agencies have tightened their standards for financial institutions. "We're a double-A credit, and we could say AmEx doesn't need capital," says Robinson. "Given the fact the name of our business is 'promises to pay,' we felt it was time to increase our strength rather than sit with the hand we had."

POSTING LOSSES. Robinson's capital-bolstering campaign began last summer. It has included everything from paying some employee bonuses in stock, which raises equity, to methodically selling off a number of assets on AmEx's balance sheet. This way, AmEx is generating more equity to support fewer assets. One plan is to securitize, or bundle into securities, as much as \$1 billion in credit and charge-card receivables so they can be sold to investors. This year alone, AmEx could reduce its assets by some \$3 billion, estimates Guy Moszkowski, an analyst with Sanford C. Bernstein & Co. "I think that will allow them to retain their rating without issuing more equity for the time being."

Most of the asset sales have been at Shearson. Despite Shearson's strong operating results in the first half of 1991, it is still posting losses from one-time write-offs. Robinson points out that between its peak in 1989 and June, 1991, Shearson's assets have shrunk by

\$25 billion, to \$66.5 billion.

Shearson is also working to improve the quality of its assets. It has already jettisoned \$1 billion in junk bonds. Shearson Lehman Mortgage Corp. is for sale. This company services mortgages, and its sale could shrink AmEx's assets by \$800 million. AmEx is disposing of \$500 million in British home mortgages owned by Shearson's Boston Co. unit. And AmEx may securitize and sell some of its \$4.1 billion portfolio of Boston's jumbo home mortgages made to affluent individuals.

In years past, AmEx was able to subsidize Shearson's persistent financial difficulties with profits from American Express Travel Related Services Co., the card division, and still have cash to spare. Those days are over. AmEx's cards are facing mounting pressure from rival cards and merchants who are demanding cuts in the fees they pay to AmEx. "TRS has momentum, but it is not robust enough to replenish AmEx's coffers," says Richard Schmidt, an analyst at Standard & Poor's.

In the third quarter, AmEx plans to securitize and sell off as much as \$1

HOW AMEX IS BOLSTERING ITS CAPITAL BASE

STOCK ISSUE	\$300 million in preferred stock sold to Warren Buffett
CREDIT CARDS	\$1 billion in card receivables may be sold
EMPLOYEE STOCK PLAN	Employee bonuses and savings-plan contributions will be paid in stock to raise \$600 million over 5 years
LOAN SALES	\$500 million portfolio of British home mortgages to be sold, along with part of jumbo mortgage portfolio
OTHER ASSETS	Shearson Lehman's mortgage unit up for sale. That could shrink AmEx's assets by \$800 million

DATA: BW

billion in TRS's \$22 billion in Optima, green, or gold credit and charge-card receivables. While the technique is old hat in the banking industry, AmEx has always remained above the fray. Says one investment banker, referring to all the administrative paperwork involved: "It's a pain in the rear. You don't do it unless you have to."

BAD-LOAN PLAGUE. Asset disposals will permit AmEx to minimize further equity sales, which could anger shareholders, whose stakes would be diluted. Last February, AmEx began paying bonuses to some Shearson employees in stock. Over five years, that and other measures, such as making contributions in stock to various employee benefit plans,

will save \$600 million through the issuance of million new shares, 5% the total outstanding.

AmEx's deal with Buffett was also designed to avoid shareholder unrest. Robinson insisted on limiting Buffett's ability to profit on the stock's appreciation. And he turned down Buffett's offer to turn his investment to \$500 million. "Jimmy, to his credit, wanted to minimize the

number of shares he was going to sell," Buffett says. "I admire him for that."

Bernstein's Moszkowski doesn't expect AmEx to issue more equity, unless "Shearson's exposures required a lot more reserves." Analysts worry about \$1.8 billion in Balcort Co. assets. The commercial real estate unit, backed with just \$200 million in reserves, has been plagued by bad loans. It has been shifted from Shearson's books onto AmEx, and it is being slowly liquidated.

Still on Shearson's books is a \$500 million bridge loan to Prime Computer Inc. And though Shearson took a \$144 million write-off in the second quarter for its stake in First Capital Holdings Corp., whose insurance units were seized by

FOR BUFFETT, AMEX IS A GREAT PLACE TO STASH CASH

If billionaire investor Warren E. Buffett needed a sobriquet, the choice could well be "Dr. Feelgood." After all, the managements of the companies in which he invests feel pretty darn good when Buffett's Berkshire Hathaway Inc. tosses a few hundred million dollars their way. He's no takeover threat, he's a long-term investor, and he doesn't second-guess CEOs. What's more, there are legions of investors, big and small, who piggyback his picks—and that gives a stock an additional boost.

The 59-year-old Nebraskan played doctor again on Aug. 1, administering \$300 million of much-needed capital to American Express Co. Buffett's purchase of AmEx's preferred shares, which would be exchanged for a 2.5% stake in the company, gives the financial-services giant access to low-cost equity capital. And it allows AmEx to raise the money without immediately diluting the equity of its common stockholders. All in all, it's a pretty good deal for AmEx.

At first glance, the AmEx deal doesn't look so sweet for Buffett and his 6,300

shareholders. The special preferred shares pay an 8.5% dividend. Period. Buffett got no promises of board seats, no voting rights, and no future discount-purchase rights. Moreover, he has no downside protection should the stock price fall below the current price of about \$25 a share. And unlike the special preferred shareholder deals he cut with Champion International, Gillette, Salomon, and USAir, there's not much upside potential.

SLIM TIMES? In fact, if AmEx's fortunes turn around fast, the investment could be short-lived. AmEx has the right to buy the stock back on a sliding scale of prices that offers at most a 37.3% profit. Even John J. "Jack" Byrne, an AmEx board member who initially pitched the AmEx investment during a telephone conversation with his friend from Omaha,

was amazed that Buffett would agree to a cap. "Mr. Buffett hates that," he declares. "His genes go against it." Buffett admitted as much in an interview with BUSINESS WEEK. "I would like to see if our upside was uncapped." But he says he ponied up for AmEx for the same reasons he invests in any business. He likes the American Express franchise, thinks he understands the business, and he knows and respects James D. Robinson III. "We're buying in with Jim," he says.

The AmEx investment doesn't look like the work of someone who made himself a billionaire and enriched shareholders, too. Berkshire Hathaway's net worth has grown at a compounded rate

23.3% a year since Buffett took over the time textile company in 1965.

But the move may be a sign that times face investors in the 1990s take a lesson from Ross A. Webb, a Wharton School professor who has styled Buffett's management style, characterized by a move as "new 90s realism. The

BERKSHIRE HATHAWAY: A HIGH-PRICED ACT





CREDIT-CARD
VERSION IS FACING
MOUNTING PRESSURE

regulators, the broker still faces an own litigation tab from lawsuits by entitled Shearson customers. Considering the enormous problems that Shearson continues to cause AmEx, analysts believe that the credit-giant may eventually decide to

dump it. AmEx denies any such plans. AmEx's current travails are a big change from its earlier days, when Robinson was hailed as a daring and innovative empire-builder. He admits that was a lot more fun than shrinking AmEx's balance sheet. But he is confronting his

current tasks philosophically. "Do I look forward to calmer days? Absolutely," says Robinson. Given the scope of AmEx's financial pressures, those days may not be around the corner.

By Leah Nathans Spiro in New York, with David Greising in Chicago

the '80s are not around any-
lolutely not."

however, warns against ana-
latest move as a portent. "For
hat's available at the time," he
There's no particular category
nent or tactic that will define
he says. "We're not interested
ies per se. We're interested in

rs seem happy enough with
latest foray. Since the AmEx
announced, Berkshire Hatha-
\$125 a share. O. K., that's not
deal as it sounds, since Berk-
thaway—the highest-priced
the New York Stock Ex-
sells at a cool \$8,650 per share.
doesn't believe in stock splits,
doesn't pay dividends. So the
in insurance, candy, encyclope-
spapers, furniture, and vacuum
plus hundreds of millions of
dividends from stocks must be

TOUGH. That, indeed, is the key
nEx deal. In a period of declin-
st rates, Buffett needs a place
his cash. The AmEx preferred
only 8.5%, but since corpora-
exempt 70% of dividend income
es, it's like earning a fat 11.6%.
asury bills yield less than 6%,

and after taxes, he'd be lucky to net 4%.

That healthy return is why Buffett is willing to forgo other sweeteners. He doesn't care about the lack of voting or purchase rights. And since he's already traveling 60 days a year to tend to the four boards on which he already sits, he's not looking to join another.

Then, with the stock market flirting with a new high again, AmEx didn't have a lot of competition for Berkshire Hathaway funds. "We find very few things we

Figuring in the tax break, the AmEx stock will pay Buffett 11.6%

really like," says Buffett. "The second half of 1990 was a lot friendlier time to find a bargain." That's when he made one of his boldest and most controversial moves—a \$289.4 million investment in Wells Fargo & Co. He bought 5 million shares, or 9.8% of the common, at an average cost of \$57.88 per share. The stock rose to nearly \$100 before concerns about Wells's exposure to California real estate sent the price plummeting. Still, the stock trades at \$70. Buffett also took

advantage of last year's bear market to take a stab at RJR Nabisco Inc. bonds—a successful first foray into the junk arena. Since junk-bond prices have rebounded this year, Buffett doesn't see any more good opportunities in that market. **'ONE GOOD IDEA.'** Despite his savvy moves last year, Berkshire Hathaway's 1990 net worth rose only 7.3%, or \$362 million. That was the smallest percentage gain in years and the closest Buffett has come to fulfilling his own 1989 forecast that Berkshire Hathaway's net worth would fall sometime before 1992. During 1990, the company's stock traded as low as 5500. Even now, after a 57% rebound from last year's bottom, the share price is still 2.5% below the all-time high of 8875 set in late 1989.

Already, 1991 is shaping up as a much better year. Three of Berkshire Hathaway's four core stock holdings—Washington Post, Coca-Cola, and discount insurer Geico—are trading at or near their 52-week highs. Only Capital Cities/ABC Inc., hard hit by the media industry dol-
drums, continues to lag.

Buffett always keeps his eyes peeled for a new investment opportunity. "Each year, I feel lucky if I get one good idea." In the AmEx investment, Buffett thinks he's got his quota for 1991 in the bag.

By David Greising in Chicago



INSURANCE

POLICYHOLDERS JUMP SHIP

The scramble is on to more stalwart insurers

How's this for dazzling ad copy? "New York Life is large, conservative, and dull." During the sizzling 1980s, such a pitch would have provoked guffaws. But in the \$1.4 trillion life insurance industry, shaken by four huge failures since spring, stodginess is sexy. Frightened policyholders are deserting sputtering highfliers to sign up with the nerds. This flight to quality is tiering the industry into haves, with assets swelling daily, and have-nots, their well-being becoming ever more precarious.

Policyholder panic was the key factor in the demise of Executive Life Insurance Co. in April and Mutual Benefit Life Insurance Co. in July, the two largest insurer failures ever. Pension funds, which invest a lot of money with insurance companies, were the first out the door. Georgia-Pacific Corp. pulled \$5.4

million from Executive Life in January, as bad news about the Los Angeles insurer mounted, sending the business to Aetna Life & Casualty Co. As the situation grew worse, individual annuity and insurance customers began checking out, too.

Like New York Life Insurance Co., the beneficiaries of these runs tend to have rock-solid investment portfolios, with limited exposure to junk bonds and real estate (table). Metropolitan Life Insurance Co., the nation's No. 2 life insurer, has long refused to buy junk. And that's paid off. So far this year through the end of July, Met's sales of individual annuities have soared 62%, to \$1.3 billion. "We like to talk about our strength," says Met Executive Vice-President Ted Athanassiades.

The very size of Met (\$103 billion in assets) and No. 1 Prudential Insurance

Co. (\$133 billion) gives them special status as havens. Sure, they are not immune from problems. Prudential suffered from its wobbly securities firm, Prudential Securities Inc., and 4.4% of Met's mortgages are in default. But they are so big that they can brush such annoyances aside. Combined, the total value of their life insurance policies exceeds that of their six largest rivals.

TEMPTATIONS. Not all of the insurers sopping up money from anxious pension executives and policyholders are beachcombers. ITT Hartford Life Insurance Co. with \$11.6 billion in assets, has no junk and no troubled real estate. In a company brochure entitled *A Profile of Stability*, Hartford President Lon A. Smith says: "Our track record is sterling—and we intend to keep it that way." Northwestern Mutual Life Insurance Co., with assets of \$31 billion, also has a pristine portfolio, because it passed up the temptation of the last decade's hot products such as universal life. Designed to compete with top-performing stock mutual funds, universal life requires hefty turns from relatively risky investments. Instead, Northwestern Mutual stays with the long-standing product that many others disdained: boring old whole life, with its unspectacular returns that often do little better than Treasuries.

There's a darker side to the story.

panies' self-congratulatory publicity signs. Some of these companies' agents are waging a shadow war with weaker insurers, stealing their clients by stressing negatives. "I tell them their company is going to hell, and they had better switch to someone more solid before it's too late," admits a New Jersey agent for a well-known, well-capitalized insurer.

Stronger carriers deny this is happening, outside of a few isolated cases. "Our CEOs don't take a tough stand with the agents in the field, so the bash goes on," complains Joseph J. Meacham, president of Equitable Assurance Society. A year last November that company was about to fail off a wave of reactions that competing insurers were happy to take advantage of. Melone says the situation ebbed in July after the insurance giant announced it would raise a \$1 billion investment fund.

Strong insurers are engaging in another form of competition: enticing agents away from their hapless brethren. Mutual Benefit admitted that 15% of its 1,200 people have left—and it's put the figure much higher. That complicates the work of New Jersey officials, who seized the insurer and tried to nurse it back to health. New York Life has picked up Mutual's leading agent, Mayer & Meyer Associates Inc. in Manhattan. "We never want to have another debacle like Mutual's exit," says President William J. Meyer. "The flight to quality is very real for us."

New York Life is just financially superior. Lee M. Gammill Jr., executive vice president at New York Life, says he has received a rash of calls from other insurers wanting to defect.

K FAX. Sales forces are the industry lifeblood, and weaker insurers are trying to keep theirs intact. After the summer rumor of its impending demise, Equitable scrambled just as hard to convince its agents that the company was O.K. as it did with the public. Says P. O'Brien, head of R. P. O'Brien & Ryer (N. Y.) insurance agency: "As soon as bad news about a company hits the paper, we get a rebuttal on fax machine."

Agents aside, the carcasses of failed insurers make good pickings for the strong. A group led by French insurer F&F struck an agreement with Califor-

nia officials on Aug. 7 to take on the well-heeled customers of Executive Life, injecting \$300 million in new capital to back up the policies. Several such healthy insurers are angling with regulators to buy the policies of other recent casualties. Met and the Pru, which have offered to help manage Mutual Benefit, may have the inside track there. In 1984, Met took over 165,000 annuity policies of failed Baldwin-United Corp. Met's Athanassiades says that this proved to be a very lucrative move.

So sensitive have insurance customers become to bad news that even the slight-

installed 32 extra phone lines to handle customer calls and rushed information packets to agents nationwide. Hancock says this worked, claiming it had no increase in policy surrenders.

NO REAL JOY. The July 25 Moody's downgrade of Kemper Corp.'s two insurance units provoked an even more aggressive response. The reason is that these insurers started at a lower, if still respectable, position: Kemper dropped from the fourth-highest rating to sixth on Moody's 20-level scale. To quell concern, the units' corporate parent pledged \$1.8 billion to bolster their capital if that's necessary.

Unfortunately for the weaker insurers, the flight to quality may have just started. Because of the continuing malaise in commercial real estate, many industry experts expect more mammoth collapses, which will further traumatize customers. "If someone five years ago had told me the average consumer would be asking about ratings, I'd have been flabbergasted," says New York Life's Gammill. Already, there is a growing amount of just-in-case switching. A nervous American Telephone & Telegraph Co., which has 2.5% of one retirement savings account with Mutual Benefit where it remains frozen under state supervision, plans to diversify new investments from its sizable defined-contribution pension kitty.

Still, the more stalwart insurers may not find the flight to quality a boon over the long term. Says Northwestern CEO Donald J. Schuenke: "If there's a loss

of confidence in a number of companies, it will spread to the entire industry." Ominously, Americans may be growing chary about insurance in general. According to International Strategy & Investment Group Inc., a New York economic research firm, insurance purchases tumbled in the year ended Mar. 30, 1991, by 8%, to \$31 billion, after years of constant increases. "Consumers probably will reduce their life insurance investments," says ISI Executive Vice-President Nancy R. Lazar. "Our guess is that they will choose Treasuries." That's a flight to quality that could make the entire insurance industry lose altitude.

By Larry Light in New York and Lisa Driscoll in Hartford, with Geoffrey Smith in Boston, David Greising in Chicago, and bureau reports

SOME STRONG INSURERS ARE GETTING STRONGER

Very well capitalized. Pays large dividends to policyholders without big high-yield investments. Good tax planner

Boasts a well-heeled parent, ITT. Has avoided junk and risky real estate investments. Asset growth outpaces industry

No. 2 U.S. life insurer has solid investment portfolio. Some real estate problems, but its size overcomes them. Has stayed clear of junk

'Large, conservative, and dull,' as its ads say. Solid, if too cautious portfolio is tilted toward high-grade corporate bonds

Stayed with plain-vanilla whole-life policies in 1980s when others pursued riskier new products fueled by speculative investments

Junk and real estate are a tiny part of the Rock's immense assets. Strategy is growing even more cautious. No. 1 U.S. life insurer is troubled by Prudential Securities, but nothing stops its surging net worth

Canada's top life insurer does one-third of business in U.S. Solid investments, with little troubled real estate, bolster big capital base

DATA: GILL & ROESER INC., BW

est cloud can be a major threat. A telling example is the recent flood of ratings downgrades that has rocked the industry. Many financial advisers lately are telling clients to stick with only the highest-rated insurers. On July 19, Moody's Investors Service Inc. yanked its top rating from John Hancock Mutual Life Insurance Co. Although the rating only went down two notches, to Aa2, the middle of the "excellent" category, Hancock

Unfortunately for the weaker insurance companies, the flight to quality may have just begun

BY GENE G. MARCIAL

A SUPERMARKET SPECIAL FOR BARGAIN SHOPPERS

As the market once again moves into record territory, analysts are scouring the landscape for a superstock in the next hot-growth area. But some pros think they may have found one in the most mundane of places—the grocery business. They're buying shares in Vons Cos., the largest supermarket chain in Southern California.

These pros describe Vons as a superior retailer that successfully tailors individual stores to each neighborhood. Its nine Tianguis supermarkets, for example, which are located in Hispanic communities, sell food and goods targeted to Hispanics. The company is also an innovative merchandiser. One gambit: "frequent shopper" cards that entitle customers to discounts on merchandise, thereby building loyalty.

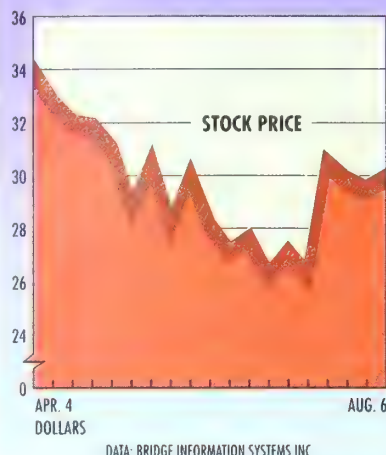
Based on earnings alone, Vons has become "a compelling buy," says analyst Gary Giblein of PaineWebber, who recently raised his estimate to \$1.80 a share for 1991 and \$2.35 for 1992, vs. \$1.28 in 1990. The stock, now trading at 29, "is undervalued and could be worth 40 over the next 6 to 12 months," says Giblein. Plus, there's a further allure: Some takeover investors say an \$80-a-share buyout is possible.

SIDE ROUTE. How so? Vons owns 328 stores, including 74 Vons Food & Drug stores and the 162 supermarkets it acquired from Safeway Stores in 1988. That deal gave Kohlberg Kravis Roberts, which controls Safeway, a 31% stake in Vons. True, KKR signed a standstill agreement that stops it from buying any more Vons shares, and the pact still has two years to run.

But the agreement doesn't preclude a friendly bid for the rest of Vons. Now that it's profitable after years of operating losses and is actively paring debt, the bet is that KKR is seriously thinking of acquiring it before August, 1993. One investor argues that even if KKR isn't interested in a Vons-Safeway deal, it could sell its 31% to another supermarket group, which could in turn pursue a merger or takeover. One possible buyer, say some pros: Great Atlantic & Pacific Tea, owner of the A&P chain, which operates mainly in the Northeast. KKR declined comment.

Vons has been busy streamlining op-

VONS: ON THE VERGE OF A RALLY?



erations after completing the integration of all those Safeway stores. Frank Prodbelsek, an analyst at Gruntal & Co., notes that Vons stores are located in the nation's fastest-growing population centers. About 75% of the stores are new or have been remodeled or upgraded in the past five years, he says, "creating one of the most modern supermarket chains in the U.S."

BIG PLANS FOR TINY CAMERAS

Laparoscopy, which enables surgeons to view the abdominal cavity and perform delicate work there through a tiny incision, has become a Wall Street buzzword for spectacular growth. So far, giants such as U.S. Surgical and Johnson & Johnson dominate the field.

But small companies are gaining entry. Medical Dynamics has attracted some big investors, which has boosted its stock from 2 in March to 7 recently. The company makes minimally invasive and diagnostic camera systems that analysts say are well-suited to laparoscopic surgery.

One of Medical's products is the 5960 surgical camera, which costs about \$14,000 and is used in a procedure that removes the gall bladder through a small incision in the navel. Bristol-Myers Squibb has purchased some \$3.6 million worth of the cameras.

Another product is the 5990 optical catheter, which costs \$20,000. It uses advanced flexible fiber optics that allow direct viewing of almost any part of the body. This camera, which is even smaller than the 5960, "can be inserted

through a needle into incisions as small as a half-millimeter and steered into previously inaccessible areas," says President and CEO Van A. Horsley. Danek Group, a major maker of spinal implant devices, has signed an exclusive pact for marketing rights to it.

Medical Dynamics "could generate sales of \$20 million in 1993," says S. Navarro of Needham & Co. He saw revenues of \$7 million this year and \$13 million in 1992, with estimated 1993 earnings of 7¢ a share and 15¢ in 1994. Navarro thinks the stock could double in 6 to 12 months.

IS PHILIP MORRIS HUNGRY FOR BORDEN?

For a stock the Street is down on, Borden is doing just fine. What's the maker of a wide variety of food products announced disappointingly flat second-quarter results on July 30, reaction was swift: A number of analysts cut their earnings estimates for '91 and '92 and slapped a sell recommendation on the stock.

Yet the shares escaped with nary a scratch. After falling from 35 to 30, Borden shot back to 35—not far from its 1991 high of 38. What's going on?

Takeover talk, that's what—within new scenarios featuring Philip Morris in the leading role. (The food, tobacco and brewery giant has often been said to be looking for another big food industry acquisition.)

One New York investment manager says "Borden is among the cheapest food companies around," given its wide range of food and specialty chemical. Despite soggy earnings and a sour outlook for 1992, Borden has "the most upside potential in the food group given the right management, says the pro. Its products include internationally known Borden dairy brands, plus Wise potato chips, New York Deli potato chips, Cracker Jacks, and Elmer's glue—all of which could use Philip Morris' marketing clout, he adds. Borden management has yet to maximize shareholder returns, he says, and "Philip Morris could certainly add value to Borden's lines." He puts Borden's takeover value at \$50 a share.

PaineWebber analyst Manny Goldman, a close follower of Philip Morris, thinks the company is just about ready to make another major acquisition. It's cash flow, he says, would allow it to extract the full value of any food company and make it click. Philip Morris and Borden declined comment.

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PLAYING 'PIN THE INSURANCE ON THE OTHER GUY'

Companies battle over health coverage for two-earner families

When General Electric Co. negotiated a new labor pact with its two largest unions on June 30, the most contentious issue was a demand that employees pay more for medical care. GE's proposal—which was accepted after heated debate—had an unusual twist. Starting next January, some 200,000 GE employees, union and nonunion alike, will pay up to \$770 a year to cover working spouses who decline the health insurance offered by their own employers. Coverage for spouses who don't work, or can't get insurance elsewhere, will cost one-third as much—\$250 a year.

GE's policy marks a new front in the battle over health insurance. The compa-

ny claims it isn't trying to penalize working couples. Instead, it's reacting to other employers that "buy out" workers—pay them to drop their health coverage and hitchhike on their spouses' GE plan. "It's not necessarily the other employee who's freeloaded" on GE, says Lawrence G. Cook, a health insurance specialist at GE. "It's the employer."

If more companies take this tack, warfare could break out among employers over who should pick up the health care tab for some 30 million two-earner families. And workers will no doubt get caught in the middle. "GE is at the far end of the spectrum at this stage," says Tom Beauregard, a health care consultant at Hewitt Associates. "But employ-

ers are increasingly trying to make sure that they don't pick up all their employees' dependents."

The immediate flashpoint is employees who deliberately try to foist their own workers and dependents onto someone else's insurance plan. Last year, the Albany City School District began offering a tempting buyout—\$1,000 a year to employees who decline coverage, and \$2,000 if the entire family drops out. The district saves big, since it now pays \$500 a year to insure a family.

HOLDING THE BAG. This year, 115 of 1,100 full-time employees took the cash. Some jumped to their spouses' plan. Others kept their insurance, but their spouses dropped off. Clara E. Backus, the district's director of food service, got \$1,000 after her husband, Edward, left the plan and took coverage from his employer, New York State. "Is it fair to buy out workers?" asks Joan C. Gold, the personnel manager for the town of Trumbull, Conn., which offers buyouts of up to \$750 a year to its 300 employees. "Other companies have the right to do it. And it saves us money."

The spread of flexible benefit plans is fueling the dependent-coverage issue.

WHO JUST WON A BILLION DOLLAR VOTE OF CONFIDENCE?



ch plans let employees choose from a nu of benefits. Currently, 52% of ge companies offer cash or other nefits to workers who decline health erage, according to a recent Hewitt vey. The upshot: Employees often in health plans at companies with xible benefits. At Citicorp, which set a flexible plan last year, more than

10% of 50,000 U.S. employees dropped the company's health insurance for covrage elsewhere.

Employers without flexible benefits, such as GE, say they wind up holding the bag. Since they can't directly influence the other companies' policies, they try to do it through their own employees. GE did soften its initial demand. Employees'

spouses who earn less than \$15,000 a year will pay nothing extra for GE health coverage, while those making \$15,000 to \$20,999 pay \$5 more a week. Everyone above that will owe the full, \$10 weekly surcharge. In some ways, that's a bargain. Procter & Gamble Co. charges \$80 a month extra for spouses who decline coverage elsewhere. Employees say the company has been doing this for several years. But P&G won't discuss its plan.

J. C. Penney Co. took one of the earliest—and most controversial—steps in 1971. It stopped covering spouses if the Penney employee isn't the family's principal wage earner. Because 80% of its 196,000 workers are female, the company has faced several lawsuits, including a class action alleging sex discrimination. Penney has won every time.

As health care costs skyrocket, more companies are likely to do buyouts. "If you don't, you end up being the recipient of everybody's opt-outs," says Gary D. Matson, manager of U.S. employee benefits at H. J. Heinz Co., which has 30,000 U.S. employees. Someone, either employer or worker, will always have a momentary edge in this game. And if everybody begins to play, the hot potatoes could be flying for years.

By Aaron Bernstein in New York, with bureau reports

MICHAEL O'NEILL/ABC



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THE COMPUTER SLUMP BECOMES A SEA CHANGE

The industry faces an age of vastly diminished expectations

When growth in the computer industry suddenly slumped back in 1985, dropping from a 15% annual rate to 9% in a matter of months, few of the largest manufacturers seemed particularly bothered. It was only a temporary downturn, they maintained, and new technologies would soon create new opportunities—and generate new profits. And business did start picking up in 1988, but not at the old rate. So industry stalwarts such as IBM, Unisys, and Groupe Bull began trimming payrolls and closing unneeded facilities. It was a calm, measured response to what IBM Chairman John F. Akers came to refer to as the market's "new reality." With a bit of fine-tuning, IBM and others figured, they could get back to customary profit levels.

Wrong. A year of recession in the U.S. has dashed any lingering hope among computer makers that things will ever again be as they were.

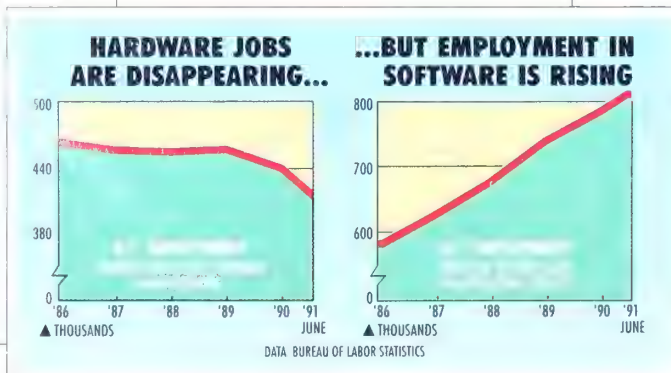
The industry is in a tremendous upheaval as it moves from dozens of hardware and software designs to just a few. Only a handful of proprietary computer "architectures"—IBM's System/390 mainframe, for one—are likely to survive.

The bulk of the market will be standards-based desktop computers, which don't require huge factories, thousands of salespeople, scores of branch offices, or even major research facilities. In short, says Charles White, vice-president for industry service at consultants Gartner Group Inc., computer hardware,

like the automobile in the 1920s, has changed from a custom-built luxury item to a mass-produced commodity. So computer makers aren't just pruning overhead—they're hacking away with a meat ax. In the heels of depressed second-quarter earnings reports—IBM's net, for example, plunged 93%—industry giants in rapid succession announced plans to lay off tens of thousands of workers. After two years of timid cutbacks, Digital Equipment Corp. set plans on July 25 to eliminate an estimated 12,000 jobs—at the cost of a \$1.1 billion charge against earnings in its just-ended fiscal year. Unisys Corp., struggling with massive debt, finally took the bold action that management says will make it profitable again: It is firing 10,000 workers and eliminating a major computer line—at a cost of \$50 million in charges. "Shave off 10% and 10% and 10%, and you go into a death spiral," says Unisys President Robert Braun.

LUCKY APPLE. All over the world, it's crunch time in the computer biz. Trailing electronics giant Philips is giving up on minicomputers, selling out to DEC. And to slash \$348 million from its operating expenses, Germany's Siemens-Nordorf Information Systems plans to cut 3,000 jobs, on top of 1,000 cut earlier this year.

There's even trouble in Silicon Valley, where desktop computer makers escaped the late-1980s slowdown. Hewlett-Packard Co. hopes to persuade 2,000 employees to take early retirement. And with cheap new Macintoshes driving down gross margins—from a high of 54% last year to 45.8% now—Apple Computer Inc. is adjusting to its own new reality. It's laying off 1,200 employees, a move that cost



1 million in the June quarter. And le and others are cutting back on s like child care and fitness centers. ut Apple is one of the lucky ones. gaining share in the still-healthy top market and has an \$890 million hoard—not to mention a promising up with IBM. Older suppliers face a y prospect: There may no longer be arket for the systems they've spent des developing. Wang Laboratories has admitted as much after years of es, layoffs, and restructurings. In e, it announced a deal to resell IBM is, which all but guarantees the de e of its own VS line.

ther established suppliers, such as ne Computer, Groupe Bull, and Con- Data, are shifting to hardware de- ed—and often built—by chip compa-. Others are banding together in sortiums such as the ACE group, led Compaq Computer Corp., which is osing a standard desktop design for to use. Norman Weizer, senior cant at Arthur D. Little Inc. in Cam- ge, Mass., says such maneuvers only y the inevitable: "The big shakeout et to come. The handwriting is on the l for a number of companies."

D THE HARDWARE. That means more gers and joint ventures. With the v economy keeping a lid on demand, e's much excess capacity in the com- er industry. Sperry fought the Bur- ghs bid that created Unisys in 1986, this year, NCR struggled to stay out AT&T's clutches. But from now on, puter makers may welcome takeover s. Even if they can cut costs and stay fitable, few have the right stuff to solo through the 1990s.

What will it take to survive? "The puterless computer company," per- s. That's the title of a provocative rvard Business Review article by An- w S. Rappaport and Shmuel Halevi. e authors, who head Technology Re- ch Group, a Boston-based consulting n, advise computer makers to simply get about building basic hardware, ich they argue is of marginal impor- ce. "Defining how the computers are d... will create real value—and thus rket power, employment, and alth—in the decades ahead," they say. lasier said than done. Software is the to giving computers true value, but remains the industry's big bugaboo— far trickier than hardware to build. expect more red ink, more cutbacks, re consolidation. "The events are pre- table. You just look at the precedents other industries," says Gartner oup's White. "It's the timing that kes the guessing game interesting."

By John W. Verity in New York, with ry McWilliams in Boston, Joseph Weber Blue Bell, Pa., and Alice Cuneo in San ncisco

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SERVICES

HIGH-TECH REPAIRS: ARE GIANTS HOGGING THE PIE?

A battle over the \$52 billion business heads for the Supreme Court



**HERNANDEZ
SAYS KODAK
"DRAINED"
HIS BUSINESS**

In the mid-1980s, ex-Marine Paul Hernandez was happily cashing in on one of the most lucrative revenue sources in high technology. His Image Technical Service Inc. in Sacramento successfully challenged Eastman Kodak Co. for the highly profitable business of maintaining Kodak microfilm and microfiche gear. By 1985, he says, he was maintaining more such gear in the state capital than Kodak was. Then, Kodak struck back. Nationwide, it stopped selling spare parts for new models to servicers. Says Hernandez: "Our business was drained dramatically."

Now, the fight between ITS and Kodak is headed for the Supreme Court and has become the focus of an intense struggle over who gets to repair all sorts of high-tech equipment—everything from computers and office phone systems to medical equipment. Indeed, a Supreme Court ruling could have ramifications in many businesses. For example, a ruling that permits manufacturers to withhold spare parts from competitors could have a major impact in the auto service business, too.

SOME BIG FRY. In high tech, the issue goes straight to the bottom line. With profit margins on product sales shrinking, manufacturers seek more money in service. They also contend that shoddy

repairs by outsiders could hurt their customers. So they're battling the outside repair outfits that they once tolerated. And they're often winning. Donald F. Blumberg, a Fort Washington (Pa.) consultant, estimates that customers may spend \$1 billion a year extra for service because of high-tech manufacturers' success in choking off competitors.

The service competitors include major independents such as TRW and Bell Atlantic Business Systems Services (formerly Sorbus), as well as big equipment makers such as Digital Equipment, NCR, and IBM. Those companies are adding service revenue by fixing other suppliers' gear. Together the outsiders have \$8 billion of the \$52 billion U.S. high-tech service market (chart), says Blumberg. He figures their share could rise 50% if the Supreme Court sides with ITS—or slide if they lose.

The path to the Supreme Court has been twisting. A federal judge in San Francisco threw out a lawsuit against Kodak by ITS and others in 1988. But an appellate panel ordered it back for trial. On June 11, the Su-

preme Court agreed to hear Kodak's appeal for dismissal. It will grant Kodak's appeal or send the matter back for trial without considering the merits of the case.

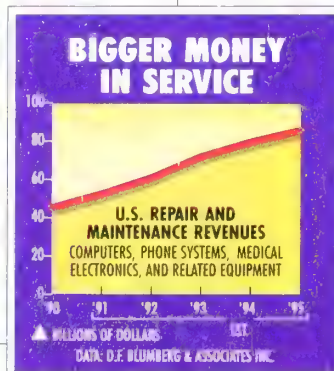
Lower courts would welcome direction from the Supreme Court. While some plaintiffs suits have been dismissed, others have hit the jackpot. Prime Computer Inc. was assessed \$25 million last year for steering customers toward hardware maintenance. Hewlett-Packard Co. had to pay \$2 million for changing the terms of maintenance contracts in a way that harmed a competitor. Four cases are on appeal. IBM has been sued by competitors, even though it makes spare parts freely available under a 1956 consent decree that ended a government antitrust suit. General Electric, Wang Laboratories, and Northern Telecom have also been enemies in legal battles with outside service companies.

Top computer makers, the Justice Dept., and the big auto makers have filed briefs on Kodak's behalf. They argue that equipment makers couldn't possibly succeed with a monopolistic strategy because if they tried to extract unreasonable profits from parts and service, word would quickly spread and customers would switch brands. The independents counter that information doesn't spread that easily, and that only a few large customers consider the cost of service in selecting equipment.

LEVERAGE. Technology is also making life harder for companies in the maintenance business. Hardware is generally more reliable now, and many machines diagnose themselves with special software that the makers zealously guard. Creating competing diagnostic software is too costly for small independents. It's a different story in Britain where outsiders do better because most customers won't buy gear from manufacturers that won't cooperate with designated third-party service companies.

Customers haven't tolerated that kind of leverage in the U.S.—yet. But if outside maintenance companies are shunted aside, the biggest losers could be their customers, who might end up paying more for service and getting less.

By Peter Coy in New York



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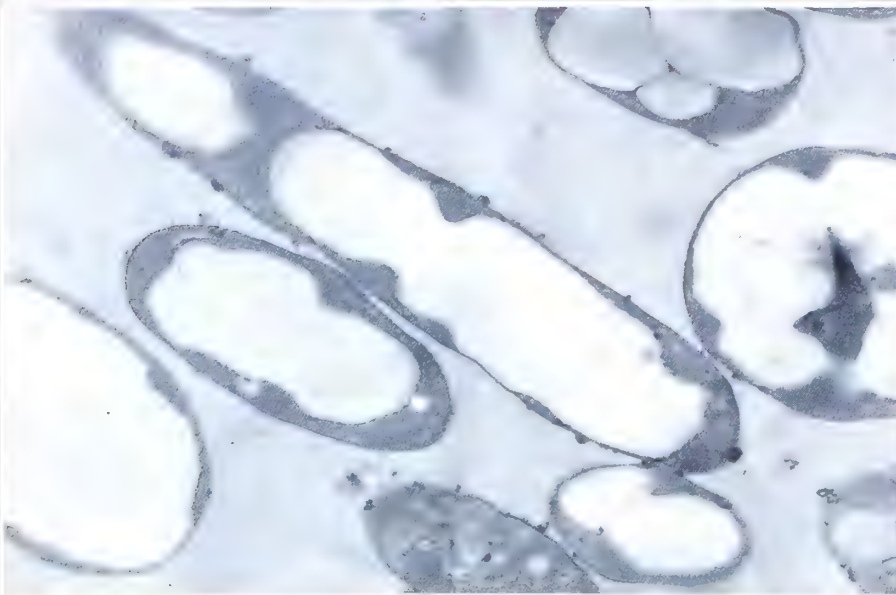
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MAGNIFIED BACTERIA: 75% OF THEIR VOLUME (THE WHITE) IS PURE POLYESTERS

PLASTICS AS HIGH AS AN ELEPHANT'S EYE?

In the future, farmers could be raising fields of plastic

Christopher Somerville has a radical notion of what a plastics factory should be. The Michigan State University professor would put his in a field. A potato or cornfield, to be exact—and its production lines would be rows of plastic-producing vegetation rising out of the earth.

It sounds like fiction, but it's science. Around the world, a growing group of researchers are studying tiny bacteria that make minute amounts of natural plastics—called biopolymers—as a food reserve. Scientists have isolated the genes that control this process, and, using the latest gene-swapping techniques, they've succeeded in turning vats of these microscopic bugs into veritable plastic-production dynamos.

Next, Somerville and others hope to insert the plastic genes into yeast, potatoes, even corn—and “grow” large quantities of biopolymers. “The productivity of plants is unparalleled,” says Somerville, who predicts that agricultural plastics could become a reality within a decade.

Plastics produced by bacteria currently cost several times more than the pennies-per-pound petrochemical versions, but they offer some big advantages.

They're truly biodegradable, for one. They also could help reduce reliance on petroleum: By combining genes from several types of bacteria, researchers in the U.S., Japan, and Germany are trying to devise polymers—chains of repeating molecules—that would replace the oil-based variety. And by inserting custom-designed genes into bacteria, scientists say they might coax out entirely new plastics, such as slowly degradable materials for use inside the body or superflexible plastics to replace rubber.

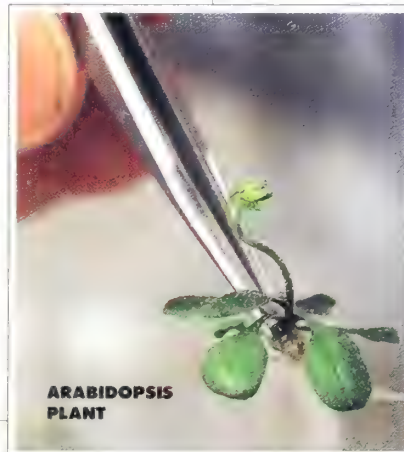
Already, there is growing commercial interest in biopolymers. In June, Britain's Imperial Chemical Industries PLC opened a plant where plastic-producing bacteria are grown in large fermenters. The plant, in Billingham, England, can produce 300 tons of the stuff annually. The price is \$15 a pound—well above the average 60¢ a pound for oil-based plastics. But this hasn't deterred

some: Wella Corp., for instance, uses biodegradable plastic in shampoo bottles to appeal to “green” German shoppers. And researchers predict that manufacturing efficiencies alone may slash the price of biopolymers to about \$3 a pound in the next few years.

Scientists have known about plastic-producing bacteria since 1925, but it was a research fluke that persuaded them that biopolymers could be commercially useful. In 1989, Douglas Dennis, a molecular biologist at James Madison University in Harrisonburg, Va., was studying *Alcaligenes eutrophus*, soil bacteria that, when starved of the nitrogen essential to its growth, produce minute amounts of a family of polymers called PHAS (for polyhydroxyalkanoates). As bears add a layer of fat before winter, these bacteria store plastic when they sense a scarcity of nitrogen or oxygen. When supplies improve, the plastic is converted into food.

GENETIC MAP. The Virginia researcher was looking for the genetic switch called a promoter, that turns on the plastic-producing genes. In the process, he transferred a long piece of DNA into *E. coli*, bacteria found in the human digestive system that are widely used for research. The bacteria immediately began churning out a plastic. Dennis had inadvertently stumbled onto the entire three-gene set that *Alcaligenes* bacteria use to make plastic. He had also proved that plastic-producing genes will turn in a new host. Dennis' good fortune set off a modern-day gold rush: Within weeks, scientists were phoning friends around the world. As a result of this work, researchers gained a vital map of the plastic-producing genes. “The technology is now available to express the genes in any organism you want,” says Oliver P. Peoples, a molecular biologist at Massachusetts Institute of Technology who is studying the complex process by which bacteria convert carbon-rich foodstuffs into polymers.

Since Dennis' find, researchers have discovered a rich diversity of bacteria that produce plastics and have begun to decipher the biological mechanisms that these bugs use to control their production. Using this knowledge, researchers at the University of Massachusetts in Amherst recently engineered a superstrain of bacteria that bulge with plastic—up to 75%



ARABIDOPSIS PLANT

ir weight. Friedrich Srienc, an Austrian chemist now leading a team at the University of Minnesota, is working on polymers that decompose in set time periods. These could be key for delivering drugs to the body.

And in Japan, Terumi Saito, a biologist at Kanagawa University, is trying to move the plastic genes into microorganisms that can produce biopolymers in sunlight. "Our aim is to improve productivity to reduce the cost" of biopolymers, says Saito.

CARBON-RICH DIET. Tinkering with genes is the only way to influence biopolymer production. Some researchers are finding plastic-producing bacteria exotic islands to come up with novel materials. For example, scientists in the Netherlands and at U. Mass. Amherst have used a rubbery PHA by feeding bacteria carbon-rich liquid octane and butane in place of sugars.

The bacteria assemble new polymers in octane "side chains" attached along their length that would be impossible to locate with petrochemicals. Because

the next step for scientists: Switching on the polymer-producing gene in crop plants

the side chains affect the strength and flexibility of the plastic, this research suggests that PHAs could replace a wide range of petroleum-based plastics in a once thought—and be useful in everything from plastic films to industrial moldings.

Bacteria are just the starting point. Last year, Michigan's Somerville coaxed three genes that produce PHA in bacteria into Arabidopsis, a tiny weed relative to the mustard plant. In January he was able to switch them all on, produce a polymer in a plant for the first time. Somerville and others say a plastic-producing crop plant isn't far off—and could revolutionize farming. "We'd like to grow corn with all these plastic genes," says Anthony J. Sinskey, an MIT microbiology professor.

The Corn Belt won't become the Plastic Belt soon. There are still some major puzzles to be solved. Scientists need to know more about the biological pathways that bacteria use to assemble polymers before they can custom-design bioplastics. Yet, biopolymers are on the way: The world's oil reserves are running out every day. And there's still plenty of room on earth to plant Somerville's field of dreams.

Gary McWilliams in Cambridge, Mass.

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Developments to Watch

EDITED BY WILLIAM D. MARBACH

MAKING FORMULA MORE LIKE MOTHER'S MILK



A major argument for nursing babies rather than feeding them by bottle is that mother's milk contains substances that are not found in infant formula. One is a fatty acid known as docosahexaenoic acid, or DHA. Some pediatricians believe that DHA is important in the rapid development of the brain in the first few months of life. Yet you

can't find it in most formulas, because there are no good natural sources of the substance.

That may soon change because of lowly algae. At Martek Corp. in Columbia, Md., scientists have found a strain of microscopic plants that make DHA. And by growing the algae in huge fermentation vats, the company can churn out large quantities of the substance, reports President Richard J. Lamer. The biosciences company is now negotiating with formula makers to supply them with the DHA.

THESE STICK-ON CHIPS MAY MAKE ASSEMBLY LINES MORE EFFICIENT

Those popular Post-It Notes from 3M Co. now have an electronic equivalent. Dallas Semiconductor Corp. has developed a chip with an adhesive underside. These Touch Memo-chips can be slapped on almost anything, such as products moving through a factory. Reading or updating the chips' data requires only momentary contact with a simple metal probe tied to a personal computer or a factory controller.

The company expects the product's main application to be linking products on production lines. Unlike bar codes and coded tags, which can't be changed, the chips can be instantly updated after each operation. They can also report their location and location to a central computer. Currently, the large-Touch Memory chip holds 4,000 bits (500 characters) and costs \$3.38.

THE FOUR-WAY RACE TO CHURN OUT ULTRAFINE PARTICLES

As scientists try to fashion a revolutionary new generation of materials for everything from high-tech ceramics to semiconductors, they are increasingly relying on ultrafine particles that contain only a few thousand atoms apiece. By linking together billions of these tiny particles, researchers design materials to be far stronger or more versatile than anything now produced. But because the particles are so hard to make, the materials remain mostly a laboratory curiosity. That's why the National Science Foundation is trying to find innovative methods of generating large quantities of ultrafine particles. Earlier this year, the agency asked scientists for their new ideas; now, it's granting \$200,000 a year for three years to each of four winning university teams. One group plans to form ultrafine materials in a plasma (an ionized gas)

and use a nozzle to control the particle size. Others will create sparks to break larger crystals into smaller ones or use tightly controlled burning to create tiny particles in the smoke. The fourth group will generate particles in a liquid solution. "Our intention is to develop the technology base for industry to use in 5 to 10 years," says NSF program manager Mihail C. Roco.

HEY, I HEAR YOU MADE VARSITY IN LBOs

When this year's crop of MBA hopefuls arrives at the University of Tennessee's College of Business Administration in a couple weeks, they'll be pioneers in what B-school Dean C. Warren Neel terms a "paradigm shift in MBA education." To foster the spirit of teamwork and cooperation that is crucial to competing in today's global marketplace, the students will study, work, and take tests in teams—and be graded primarily on their performance as team players.

The emphasis on teamwork applies to the faculty and curriculum, too. Instead of teaching their own classes, 10 professors, dubbed the A Team, have agreed to jointly teach a first-year course that will stress the overlapping and interdependent functions of modern business. In haggling over the new course, the A Team was forced to admit that traditional MBA programs concentrate too much on narrow specialties. To develop a broader sense of leadership in students, the new curriculum includes less economics, a lot less statistics—and more of the dynamics of the real business world.

The Tennessee program is a bellwether. This summer, the American Assembly of Collegiate Schools of Business, a St. Louis organization that accredits B-schools, revised its curriculum standard. In the future, all MBA candidates must receive more training in technology and a better grounding in the cross-disciplinary nature of global markets and companies.

CHIPMAKING TOOLS THAT TIDY UP AFTER THEMSELVES

There's nothing quite like the manufacturing challenge facing the semiconductor business: The process is so delicate that contaminants too small to be visible under optical microscopes can ruin a chip. Even on the best fabricating lines, at least 20% will turn out to be defective. IBM Corp. estimates that worldwide, defects caused by contaminants cost the industry more than \$1 billion a year.

Chipmakers and semiconductor-equipment companies have focused on improving clean-room quality and the purity of processing chemicals. Now, new research by IBM scientists points in a different direction: self-cleaning chipmaking tools.

The researchers used laser light to peer inside the vacuum chambers of plasma tools used in chipmaking. They found that during normal operations, a cloud of microscopic contaminants drifts over the silicon wafers on which the chips are made. They also discovered that a relatively inexpensive design modification of the tools could reduce the problem. In effect, the contaminants can be deflected away from the wafers—into an electrical "drainpipe"—and pumped out of the tool.



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With an Introduction by Jim Brady

ISSUE DATE: October 28th, 1991 • CLOSING DATE: September 16th, 1991

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FIELD OF SCREAMS

It's a yuk a minute at Salinas Spurs games. Baseball is played, too

The hometown Spurs aren't even at bat when the crowd lets loose its biggest roar of the night. The 489 fans at Municipal Stadium in Salinas, Calif., are watching one of many between-innings entertainments: Two fans lean over, put their noses to an upright bat, and spin around it 10 times. Then, they try to run to first base. One keels over at once. The other staggers to the bag. Oh, and the Spurs lose, 10-2, to the San Jose Giants.

Welcome to one of baseball's odder outposts, where cornball contests are as big a draw as baseball. Bigger sometimes, because frankly, the Salinas Spurs, cellar dwellers of the Class A California League's Northern Div., aren't all that great. With few major-league prospects on the roster, the Spurs lose twice as often as they win. Some nights, they are lucky to draw 250 people to the chilly, foggy, 44-year-old stadium. Moans Spurs General Manager Kevin Haughian: "If you asked 10 people in Salinas who the Spurs are, three wouldn't know, and seven wouldn't care."

YUPPIE OWNERS. That's particularly frustrating when many of the nation's 170 minor-league teams are as prosperous as they've been since the 1940s, before television beamed big-league baseball into the smallest towns. Thanks to smart marketing—and the 1988 hit film *Bull Durham*—attendance has rebounded to about 20 million a year, double the low point hit in the 1960s.

Moreover, heightened interest in baseball ownership among rich yuppies and celebrities—from Billy Crystal to Jimmy Buffett—has pushed franchise values sky-high. Even the Spurs are worth nearly \$1 million today, by some estimates, up from \$13,500 a decade ago.

How can such a sad-sack team be worth so much? "There are more millionaires interested in sports than there are minor-league teams," explains Haughian.

Bedazzled would-be owners, though, should hearken to the headaches of Kat-suaki "Don" Nomura, a Los Angeles and Tokyo real estate developer who owns the Spurs. One reason fans stay home is that Municipal Stadium is short on amenities. Toilets back up whenever

also has a unique arrangement to use 10 players from two major-league Japanese teams, the Daiei Hawks and the Yakult Swallows. They pay for Japanese players' salaries, hotel room and meals, plus \$10,000 per player.

DEPRESSED. The Japanese rookies prove the bottom line, if not the on-field performance. The Spurs' batting average is only .240, and its 5.30 earned run average is the league's worst. It's all a bit depressing for players such as Jim Eppard, a 31-year-old former baseman for the Toronto Blue Jays and California Angels. He doesn't have major-league power, but he hopes his average will land him a job in Japan and get him out of Salinas. "It's tough to get psyched up to play here," he says.

Haughian, a 32-year-old former California legislative aide, somehow keeps up his enthusiasm for luring fans to park. He dreams up 13 promotional



NEED GLASSES? AFTER A BAD CALL, A SPURS FAN RIBS THE UMPIRE BY HANGING OUT AN EYE CHART

the Spurs draw 1,200 or more. With inadequate electricity, Haughian can't even cook French fries, severely limiting food concessions that make up more than half of revenues and all the profits.

Not coincidentally, community and business support is hard to come by. The fans who do show up are part of the show. The leader of the 122-member Spurs booster club, Dale Hooper, often holds up an eye chart to umpires when they make a bad call.

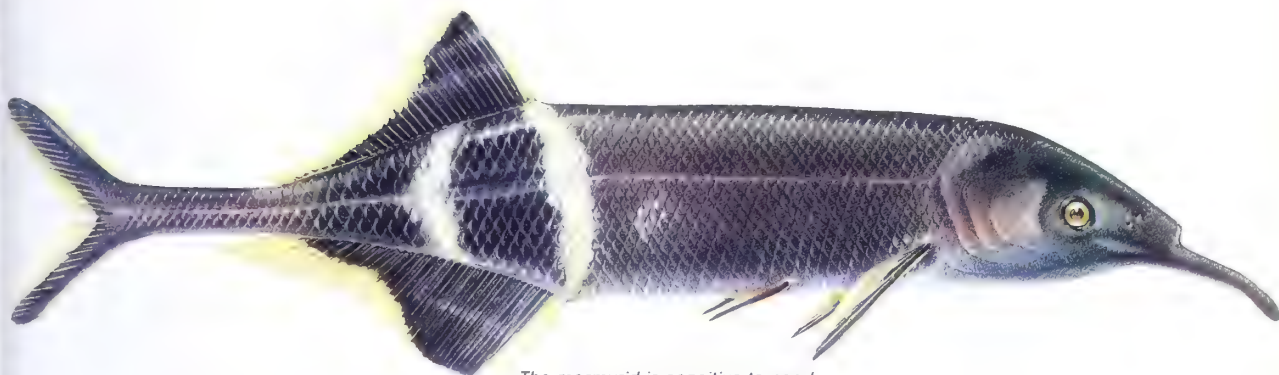
The players sometimes provide more comic relief. Since the Spurs are one of the few minor-league clubs without a major-league affiliate to provide players and pay their salaries, Haughian must rely on rejects from other teams. He

game, ranging from bingo to Pizza Party Polka: To the strains of a bad pop record, a fan runs to one of the bases. Under it lies a gift certificate for pizza or Spurs souvenirs—or a big prize, such as an autographed photo of the groundskeeper.

The antics are paying off. Attendance has tripled from last year, to an average of 900 a game, which may net a small profit. But more than money keeps Nomura in the game. There's family loyalty, too: His stepfather manages the Swallows. "Baseball blood runs through my body," he declares. That's nice, but he might help the team more if he had a decent fastball.

By Robert D. Hof in Salinas

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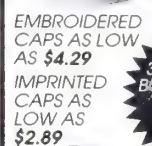
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EDITED BY AMY DUNKIN

Insurance

WHAT IF YOU CAN'T WORK?

Most people build a solid nest of insurance, papering it with policies on their life, health, home, and car. But many fail to protect what enabled them to buy all that coverage in the first place: their income. Disability, or "lifestyle," insurance ensures that if you become disabled for a long stretch, you won't be hit with a sharp drop in income as well. While your employer may provide some long-term coverage, it's often not enough and—given the prodigious amount of jargon used—not well-understood.

"Disability is the most overlooked coverage there is," says Steven Ross, a financial planner with IDS Financial

Services in Arlington Heights, Ill. For someone aged 35 to 65, the chances of being unable to work for 90 days or longer because of a disabling injury or illness are about equal to those of dying, says the Health Insurance Assn. of America. And many more homeowners face mortgage foreclosure because of disability than because of death. Yet people are far more likely to buy life insurance than disability coverage.

MONTHLY CAP. Most medium and large companies offer employees some form of short- and long-term disability coverage. In a typical long-term plan, an employer will pay 50% to 60% of the pretax salary—but will cap monthly pay-

ments around \$5,500. That means anyone earning into the six figures may find the income from their company's group plan inadequate.

A company's short-term disability plan usually provides 70% to 80% of pay up to 13 or 26 weeks. The typical waiting, or "elimination," period between the end of short-term and the start of long-term benefits is six months. And since you won't receive a check until a month after that, you'll have to cover seven months' expenses out of personal savings and other benefits.

If your employer shoulders the premiums, any payments you receive are taxable. If you foot the bill, you're pay-

ing with aftertax dollars, the benefits are tax-free. "People ought to ask whether it's worth paying premiums themselves, which may amount to 0.4% to 1% of their pay, or having an employer pay, but being taxed on the benefits," says Bob Schilmeister, a consultant at the New York office of benefits consultants Towers Perrin. In a group plan, where you have no say in plan design, you may not have a choice. In flexible, "cafeteria" benefit plans, however, you may have payment options. **STRICT DEFINITION.** Before you can determine if you have enough disability coverage, you need to figure out what your expenses would be

were unable to work. When you determine what you'd live on comfortably, evaluate what other benefits it kick in. This may include disability payments from a defined-benefit pension plan or payments from Social Security. But Social Security definitions of disability are so stringent that "we suggest that people don't count," says Steven Weinstein, partner with Arthur Andersen in Chicago.

The first question to ask about a plan is what definition of disability is being used. "Own occupation" or "regular occupation" policies consider you disabled and eligible for benefits if you cannot work in your own occupation. "Any occupation" policies consider you disabled if they cannot perform any work for which they are qualified by education, training, or experience. Group policies often define "own occupation" coverage for the first year or two of disability and then switch to "any occupation." You can buy individual policies that stipulate coverage until age 65, or for life, but the cost may be prohibitive. You can also buy policies that pay benefits for 1 year, 5 years, or 10 years.

Another important consideration is whether your policy requires that you be totally disabled before you qualify for benefits. "Often, as long as people are partially disabled, they are not eligible for benefits," says Jill Madison, a principal with benefits consultant William M. Mercer. Some employers are starting to look at that issue, especially in California with AIDS. You may not be able to work every day, but they're not totally disabled."

IN SHORTFALL. If you think your company's age is enough, you may be able to buy supplemental coverage through your company plan. "The cost is probably 10% less than you'd pay for it on the outside,"

says Madison. The cost ranges from 20¢ to 39¢ for \$100 of additional coverage. While you may be able to offset another 20% or so of

your income this way, it's unlikely that you'll ever be insured for more than 80% of your income. "Insurers don't want you to end up being paid more on disability than when you are being an income-producing member of society," says Connie Chen, president of Chen Planning Consultants

Sign on when you're young, and you'll lock in a lower premium

in New York. If your employer doesn't offer supplemental coverage, a professional association may.

One big drawback to group policies: You can't take them with you if you leave your company. For a partial safeguard against that, or just as a supplement to a group policy, consider

an individual disability policy. "Many highly paid people like this as a security measure," says Schilmeister. "They say at least it's a fall-back."

Individual policies, while far more expensive than group coverage, can pay monthly benefits as high as \$25,000. And they have more liberal definitions. Most are noncancelable, meaning that as long as you pay your premiums the policy can't be canceled, regardless of your health.

A policy that you buy on your own may also have a partial, or "residual," disability provision built in or available at extra cost. So if you return to work partially disabled and can't work every day, or have to take a lower-paying position, the policy will fund the shortfall, usually if your drop in income is 20% or more. That can be important for owners of small enterprises who can't go prospecting for busi-

ness. One snag is that you have to qualify for this coverage, and if you have a preexisting condition, you may run into problems.

While the features offered in basic policies differ among insurers, the high cost is a constant. Consider a 40-year-old nonsmoking executive who wants to receive full benefits if unable to return to his or her occupation. With a salary of \$100,000 a year, the executive might pay a monthly premium of \$145 for a policy that replaces almost 60% of salary, to the tune of \$4,700 a month, according to Provident Life & Accident Insurance. In this example, the executive has to be disabled for 90 days before the policy kicks in, and the policy will run to age 65.

BUY YOUNG. The longer you wait to buy a policy, the more expensive it will be. Insurance companies increase the premiums about 4% a year until about age 50, when premiums can jump 7% to 10%, says IDS' Ross. So it pays to buy young. If you purchase a policy at age 35, for example, when premiums are less expensive, you're locking into that lower price.

If you buy a policy on your own, you'll be faced with a bewildering array of add-on options, or riders. Most are costly. They include cost-of-living adjustment (COLA) riders, which may increase potential payouts by a set percentage each year or track the actual increase in the cost-of-living index. Future purchase options are also offered, allowing you to buy additional coverage on your policy even though your health may have declined. (For more information, write the Health Insurance Assn. of America, P. O. Box 41455, Washington, D. C., 20018, for a free booklet, *The Consumer's Guide to Disability Insurance*.)

Of course, choosing a top-quality insurer is the first step in shopping for coverage. What you're buying is a promise to pay—and you can't afford to have that promise broken if you become disabled. *Suzanne Woolley*



UNDERSTANDING A DISABILITY POLICY

- Find out how your insurer defines disability. Will you be eligible for benefits if you can't work in your occupation only, or must you be unable to work in any field for which you are qualified by "education, training, or experience"?
- Check whether you must be totally disabled before benefits begin. Some policies provide benefits for partial disability—if you can't work every day, for example—but usually only if it follows a period of total disability for the same cause.
- Make sure the policy covers you for sickness, not just accidents. You are more likely to need disability coverage for illness than for injury, especially after age 50.
- Be sure an individual policy is noncancellable. That means that as long as you pay your premiums, the policy cannot be cancelled, regardless of any decline in your health.

Education
www.entrepreneur.com

B-SCHOOLS THAT LET YOU TELECOMMUTE

While living in Charlotte, N.C., Grady Walters enrolled in a weekend business administration program for executives at a local school. Five months later, the Otis Elevator manager was transferred to Tulsa and lost all his credits. Not wanting to repeat the experience if he had to move again, he signed up for an unusual course at Purdue University.

Unlike conventional programs that hold classes every other weekend, Purdue requires executives to show up at the West Lafayette (Ind.) campus for six two-week periods over two years. Students set aside the two-week blocks well in advance with their employers' permission. The rest of the time they study at home, staying in touch with



professors and classmates by computer and fax machine. They spend roughly 20 hours a week on schoolwork.

NO GYM. By removing the bi-weekly commitment, Purdue and two other schools make geography largely irrelevant. "It appeals to people who need flexibility in their career paths," says Skip Gross, who directs the University of Pittsburgh's program.

True, you don't see your professors that often, and you

won't be able to use the university's library or gym. But pros make a point of returning phone calls within a couple of days. And the two weeks on campus—with all business and family matters left behind—are intense. "You leave there hamburger meat," says Walters, who graduated this past spring.

Purdue emphasizes quantitative subjects such as finance, and it awards students an MS in management. Pitt

and Bowling Green State Ohio offer an MBA with a general-management slant. Applicants must have worked for 12 years and taken Graduate Management Admission Test. For Pitt, applications must be in by Jan. 1. Purdue and Bowling Green apply in the spring.

None of these programs is cheap—though employers usually foot the bill. Purdue charges \$25,500—about the cost of Harvard's full-time MBA program—and you have to buy a Macintosh computer setup that can cost \$3,000 more. Pitt's program will cost you or your company \$28,500, and you'll have to cough up airfare for a week tour of companies in Europe. Then, there's the cost of commuting. Some executives at Purdue fly in from as far away as Albuquerque, N.M., and Puerto Rico.

While balancing job and school, expect to put your personal life on hold. If you go to school full time or weekends, these programs offer a way to earn what might be considered business' gold passport. *David Leonhardt*

For safety, there's nothing like a money market fund that invests solely in U.S. Treasury bills. But the current yields, barely above 5%, are unappealing—especially after paying federal taxes. Now, two funds, the Permanent Portfolio Treasury Bill Fund and the Eaton Vance Short-Term Treasury Fund, help delay the tax bite.

Unlike conventional money funds, which keep their share value at \$1 and pay interest daily, the tax-deferred funds retain the interest, so net asset value goes up a little each day. Investors earn their return through the appreciation.

SMALLER TAB. Shares in the Permanent Portfolio fund climbed 3.1%, to \$64.79, from yearend through July 31. The 5.3% annualized gain is about the same return as that of conventional T-bill funds. The difference is, investors in regular funds will

Smart Money

TREASURY FUNDS TO DEFER THE TAX BITE

owe full 1991 taxes on the interest, while Permanent Portfolio investors will owe a small amount, if any. "Your interest compounds tax-free," says Terry Coxon,

Investors won't owe the IRS until they sell their shares

who runs the \$300 million fund.

These funds comply with federal rules that mutual funds pay out all income. They do so via a complex accounting method that allows

them to minimize reported income. For instance, in December, 1990, the Permanent Portfolio paid out 43¢ per share, or 0.6% of net asset value, while the fund had a total return of 7.3%. So most of the return was deferred. In 1987 and 1989, there was no reported income. So holders who didn't redeem shares didn't pay taxes. The new Eaton Vance fund isn't yet a year old, but "the distribution will be less than with a conventional T-bill fund," says Executive Vice-President James Hawkes.

LONG-TERM TIP. For taxpayers in the highest brackets, there's an additional savings. As long as their shares are

held for more than one year, they qualify for long-term capital gains tax treatment. That's a plus, since the maximum tax rate is 28%, vs. as high as 34% on ordinary income and short-term gains. And investors can use capital gains in these funds to offset capital losses.

There are a few drawbacks. Each withdrawal is a "taxable event" which needs to be reported to the IRS. Coxon's fund has a \$1,000 minimum purchase. It charges \$35 to open an account, a \$1.50 per month maintenance fee, and \$10 a check. The Eaton Vance fund has a \$5,000 minimum and a 0.25% distribution fee.

Finally, both funds' yields run about half a percentage point below the three-month T-bill rate. But the security and tax deferral attached to these investments may make up for the relatively skimpy returns. *Jeffrey Laderman*

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**The Guardian's ratio of speculative grade bonds as of 3/31/91 was only 1.2% of assets. The ratio to capital was only 8.6%. Capital equals surplus plus MSVR.

***Moody's capitalization ratio of 14.6%; surplus plus MSVR plus 50% of dividend reserve liability divided by assets as of 12/31/90.

****Equity products are offered through Guardian Investor Services Corporation, a wholly owned subsidiary of The Guardian Life Insurance Company.

Hotels

D.C.-BOUND? TRY AN OLD VIRGINIA INN

For most executives, a trip to Washington falls into a familiar pattern: a shuttle flight to National Airport, a blur of meetings, and occasionally a stay at one of the city's grand old hotels.

The next time you find yourself in the nation's capital, consider a serene alternative to the city's hubbub: a weekend getaway at one of the historic inns that dot the Virginia countryside.

The region's premier attraction is the popular Inn at Little Washington (703 675-3800). Located in the quiet village of Washington, Va., about an hour away from its larger namesake, the inn offers superb French-inspired cuisine as well as a world-class wine list. The rooms feature ele-



CHARLOTTESVILLE'S BOAR'S HEAD INN: A HEALTH CLUB, FOUR POOLS, 17 TENNIS COURTS—AND HOT-AIR BALLOON RIDES

71-1800), a restored plantation once owned by Thomas Mann Randolph, Thomas Jefferson's son-in-law, offers large rooms furnished with antiques and a wood-burning fireplace. Situated on 35 wooded acres, the inn has a private lake and miles of walking trails. Dinner is not served, but a full breakfast is included in the room price, starting at \$138.

Woodstock Hall Inn (804 293-8977), a 1757 roadhouse 10 minutes west of Charlottesville in Ivy, Va., has atmosphere galore. Restored down to its antique locks and handmade light fixtures by sisters Jean Wheby and Mary Ann Elder, Woodstock is small and homey. Rates start at \$95, with a cottage available for \$130.

For those who demand amenities, Charlottesville's Boar's Head Inn (800 476-1988) is a full-scale resort that boasts a health club, four pools, and 17 tennis courts. A private golf course is nearby. The modern rooms are spacious and well-appointed. For

a panoramic view of the countryside, you can sign up at the front desk for a ride in a hot-air balloon (\$125 an hour). Three restaurants serve up delectable fare, such as roast

goose Shenandoah. The hearty Sunday brunch—featuring country bacon, seafood specialties, and home-baked pastries—is a bargain at \$12.95. Rooms start at \$105, suites at \$170.

TEATIME. Want more peace and quiet than even Charlottesville can offer? Get thee to Mayhurst (703 672-5597). About 90 miles from Washington in tiny Orange, Va., the stunning Victorian Italianate manse is perched high atop a hill. The peaceful grounds include a pond, hiking trails, and an antique shop



run by congenial innkeeper Shirley and Stephen Ramo. There are only seven guest rooms, each beautifully furnished with antiques. Afternoon tea is served, and country breakfasts are featured. Rooms start at \$95.

At most of these rural hotels, you can't watch CTV, use a fax, or even make a call from your room. What you will get is a sense of history, the quiet majesty of the Virginia countryside, and a special calm that comes from leaving Washington's noise and factory behind. *Jane Todd*



THE MAYHURST IN ORANGE: ALL SEVEN GUEST ROOMS ARE FURNISHED WITH ANTIQUES

gant decor by Joyce Evans, a British theatrical designer, and most have window seats or private balconies. The elegance doesn't come cheap: Dinner for two can run \$250; a room goes for \$290 to \$380. Book well in advance.

PRIVATE LAKE. You can find many beautifully restored historic guest houses in and around Charlottesville, 112 miles from Washington, in Virginia's tony Albemarle horse country. Clifton (804

Worth Noting

MIGHTY QUINN. Personal finance expert Jane Bryant Quinn instructs you in *Making the Most of Your Money* (Simon & Schuster, \$27.50). The cradle-to-grave guide is due out in late August.

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nounces the status of flights into and out of most major airports—a boon when airplane phones are clogged.

EARTH BONDS. A new free muni fund invests in high-grade California bonds for education, housing, and the environment. The Muni Fund (800 648-3448) is run by "ethical" investors who plan a national fund.



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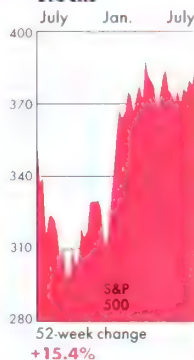
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Investment Figures of the Week

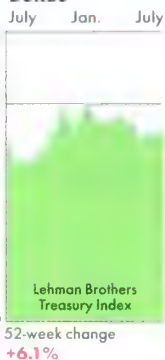
COMMENTARY

Rising interest rates set the tone for the week, boosting bond stock prices—at least for a while. On Aug. 6, the Federal Reserve moved to cut short-term interest rates, and the Dow Jones industrial average reacted by rising 38 points to 3027. That was just shy of an all-time record. The rally fizzled out the following day. The dollar followed interest rates downward, as did prices. Indeed, gold mining shares have lost one-tenth of their value in the past month.

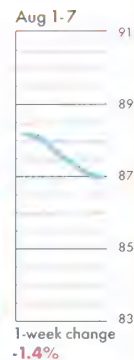
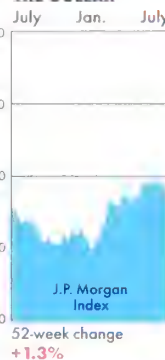
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS	Latest	% change Week	% change 52-week
JONES INDUSTRIALS	3026.6	0.1	10.7
COMPANIES (Russell 1000)	204.2	0.7	16.7
COMPANIES (Russell 2000)	173.1	0.2	14.5
COMPANIES (Russell 3000)	216.7	0.7	16.6

HIGH STOCKS	Latest	% change (local currency) Week	% change 52-week
FINANCIAL TIMES 100	2597.4	0.3	16.1
NIKKEI INDEX	23,691.0	-1.8	-16.9
TSE COMPOSITE	3528.6	-0.3	1.5

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.53%	5.67%	7.6%
30-YEAR TREASURY BOND YIELD	8.18%	8.34%	8.9%
S&P 500 DIVIDEND YIELD	3.2%	3.1%	3.5%
S&P 500 PRICE/EARNINGS RATIO	19.9	19.7	15.7

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 26-week moving average	376.6	375.1	Positive
Stocks above 26-week moving average	55.0%	54.5%	Neutral
Speculative sentiment: Put/call ratio	0.36	0.41	Neutral
Insider sentiment: Vickers sell/buy ratio	3.32	3.18	Negative

INDUSTRY GROUPS

4-WEEK LEADERS	% change 4-week	% change 52-week
EQUIPMENT AND SERVICES	16.7	-10.5
TOES	14.2	45.7
SMETICS	13.5	30.6
NANCE	13.1	26.1
HOUSEWARES	13.0	44.1

4-WEEK LAGGARDS	% change 4-week	% change 52-week
OLD MINING	-10.3	-25.0
MEBUILDING	-9.9	16.5
GINEERING AND CONSTRUCTION	-8.7	1.8
ITOMOBILES	-7.4	-10.6
OD CHAINS	-5.8	8.6

Strongest stock in group	% change 4-week	% change 52-week	Price
SCHLUMBERGER	21.2	3.7	70
REEBOK INTERNATIONAL	20.0	103.5	29 1/4
GILLETTE	18.8	37.1	41 1/8
AMERICAN EXPRESS	22.3	-3.6	26 3/4
PREMARK INTERNATIONAL	31.6	48.3	32 1/4

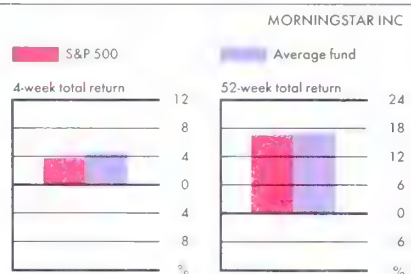
Weakest stock in group	% change 4-week	% change 52-week	Price
NEWMONT MINING	-11.9	-28.0	36 7/8
KAUFMAN & BROAD HOME	-15.3	17.5	11 3/4
FLUOR	-11.3	0.0	43 1/4
FORD	-9.4	-18.2	32 3/8
KROGER	-14.4	25.2	18 3/8

MUTUAL FUNDS

LEADERS	Week total return %
EQUITY STRATEGIES	16.7
ARTWELL EMERGING GROWTH	14.0
ILL & BEAR SPECIAL EQUITIES	13.7

LAGGARDS	Four-week total return %
STRATEGIC INVESTMENTS	-17.3
STRATEGIC SILVER	-14.6
UNITED SERVICES GOLD SHARES	-11.8

Week total return %	52-week total return %
DELITY SELECT BIOTECHNOLOGY	73.2
DELITY SELECT MEDICAL DELIVERY	68.1
FINANCIAL STRATEGIC HEALTH SCIENCES	64.6
STRATEGIC SILVER	-32.9
RUSHMORE PRECIOUS METALS INDEX PLUS	-30.3
STEADMAN OCEANOGRAPHIC TECHNOLOGY	-28.5



RELATIVE PORTFOLIOS

For amounts present the present value of \$10,000 invested one year ago each portfolio percentages indicate day total returns


U. S. stocks
\$11,777
+1.02%


Treasury bonds
\$11,165
+2.43%


Money market fund
\$10,594
+0.11%


Foreign stocks
\$9,493
+1.21%


Gold
\$9,446
-1.20%

Data on this page are as of market close Wednesday, August 7, 1991, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of market close

August 6. Mutual fund returns are as of August 2. Relative portfolios are valued as of August 6. A more detailed explanation of this page is available on request

GIVING YOUNG AMERICANS A SQUARE DEAL

For many decades, most Americans could count on the strength of U.S. industry to make them increasingly prosperous throughout their lifetime. Even those people who never finished college—three of every four adults—were able to enjoy high-paying jobs, usually in manufacturing. But the American dream isn't coming true for young people today. Families with breadwinners under 30 earn less than similar families did in 1973, after inflation is taken into account. Worse, they face the dispiriting prospect of never matching, much less surpassing, the lifestyles of their parents. If that happens, they will be the first generation of Americans to fall behind their parents (page 80).

The causes of the malaise stretch back over decades, so solutions can't be implemented overnight. A major problem is that many American companies are not creating the high-skilled jobs that would allow them to pay a decent wage. In manufacturing, stiff international competition has forced companies to clamp down on pay. Now, employers are realizing that quality is a key to regaining U.S. competitiveness against global rivals. But to achieve that competitiveness, companies must increase their skilled work force, which is increasingly hard to come by. The U.S. lacks the kind of formal training and apprenticeship systems that countries such as Germany use to help workers not bound for college. Companies and government officials have been making some progress on this score in recent years. But a much more intensive effort is needed to help young workers make it in today's new manufacturing environment. Experts say that

private industry should be spending anywhere from 3% to 6% of payroll on training, compared with the 1.4% average that companies now spend.

The problem is more subtle, and hence even tougher to solve. The measurement of productivity in service industries is difficult, but the available numbers suggest that productivity is stagnant. Because service industries produce little more per worker than they did 30 years ago, employers can't afford to pay wages that keep pace with rising living costs. Again, the quality of the work force is key. But for most service jobs, it's a high-quality education rather than technical skills, that is important. This means that U.S. schools play a crucial role in Americans' economic prowess. Educational reform has been a growing issue since the mid-1980s. But the efforts so far are largely piecemeal. If Americans don't want to condemn young people to a declining standard of living, they must get serious about fixing their school system.

The good news is that the time couldn't be better for such solutions. Many economists expect the labor and skill shortages that began in the late '80s to reappear after the recession and to continue throughout this decade. Employers won't be able to rely on a surplus of workers to fill jobs. Even service companies will be forced to find some way to produce more with fewer people. This gives the U.S. a unique window of opportunity. If America can supply workers who are sufficiently trained or educated, employers will be able to use them—and pay them more.

DEEP-SIX THE MISSILE DEFENSE ACT

When the House of Representatives reconvenes in September, it should make shooting down the Missile Defense Act a top priority. The Senate-backed legislation would commit the U.S. to deploy an antimissile-defense system at Grand Forks, N.D., by 1996. It would also direct the President to open talks with Moscow to amend the 1972 Anti-Ballistic Missile Treaty, a cornerstone of U.S.-Soviet deterrence, to permit additional antimissile sites and space-based missile-detection sensors.

The proposal, hatched by Senator Sam Nunn (D-Ga.), is long on politics and cost—as much as \$60 billion as envisaged—but all too short on policy. Nunn argues that new ground-based missile defenses are needed to protect the U.S. against accidental or unauthorized launches by the Soviets or a terrorist attack by the next Saddam Hussein. But chances of an accidental launch are no greater now than in the past. And why would a breakup of the Soviet Union tempt a rogue Soviet general or nationalist clique to invite certain and devastating retaliation? For the same reason, fears of Third World ballistic launches against the U.S. also are overblown. Short-range attacks by developing countries,

against their neighbors as well as the U.S., are a great threat—but Nunn's system would be ineffective against them. No wonder the Federation of American Scientists opposes the proposal "a capability in search of a mission."

If the U.S. deploys nationwide antimissile defenses, the Soviets will likely do the same. Setting Moscow off on a costly round of missile-building would make a mockery of U.S. calls for the Soviets to cut back on defense and convert military facilities to civilian use. It could undo nine years of talks to slash superpower nuclear arsenals: The Soviets have long warned that they would walk away from the Strategic Arms Reduction Treaty if the U.S. breaks the ABM Treaty.

The U.S. would be foolish to tamper in this way with the ABM treaty. Treaty framers recognized that widespread deployment of antimissile missiles by one side would lead the other to enhance its offensive forces to overcome the defenses. A spiraling defensive-offensive arms race would ensue. The Senate seems to have forgotten a key tenet of deterrence: Country A will not launch a nuclear attack on Country B if Country A doesn't think it can snuff out any certain retaliatory blow by Country B.

BusinessWeek

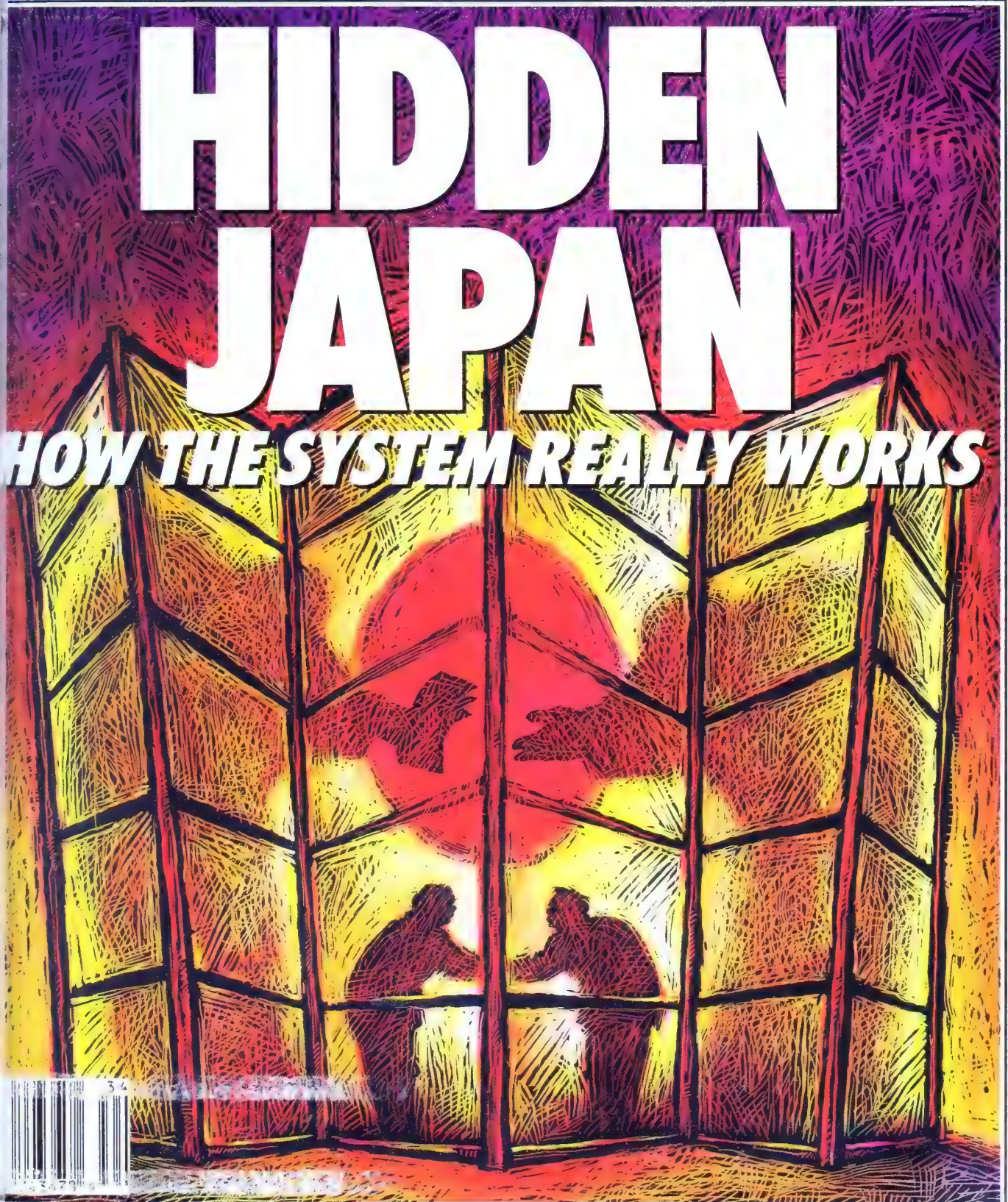
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HIDDEN JAPAN

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PYRAMID OF PAYOFFS? JAPAN'S SCANDALS ARE GIVING OUTSIDERS WHO WANT TO DO BUSINESS THERE A LOOK AT WHAT THEY'RE UP AGAINST

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The current scandal is exposing how politicians, bureaucrats, big business, and even gangsters work together to keep Japan's economic engine primed. Deals that would be illegal elsewhere are simply business as usual. Once again, a troubling question arises: Is Japan's system compatible with the rest of the world's?

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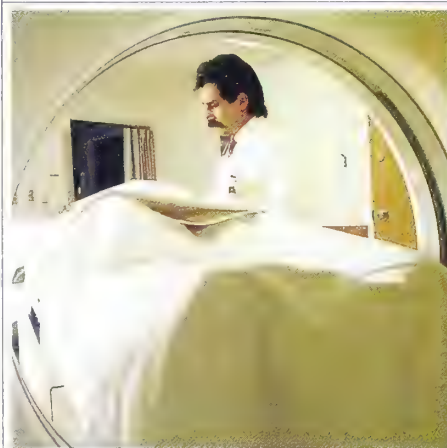
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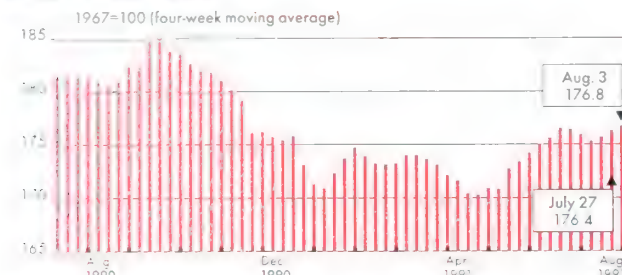
Salomon is not too big to punish
Japan must clean its own house
When business should mind its own

BusinessWeek Index

PRODUCTION

Change from last week: 0.2%

Change from last year: -1.9%



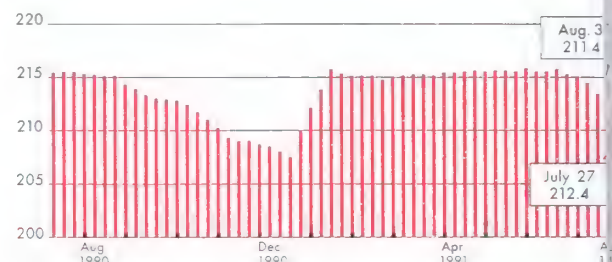
The production index increased slightly for the week ended Aug. 3. Seasonally adjusted output of autos and trucks fell as some plants closed to switch over to new 1992 car models. Electric power, crude-oil refining, coal, paperboard, and rail-freight traffic output also declined. Steel and paper production increased, and lumber output was unchanged. Before calculation of the four-week moving average, the index fell to 174.1, from 178. In July the index dropped to 176, from 176.5 in June.

BW production index copyright 1991 by McGraw-Hill Inc.

LEADING

Change from last week: -0.5%

Change from last year: -1.9%



The leading index edged lower during the week ended Aug. 3. Materials prices continued to deteriorate for the sixth consecutive week, and growth in real estate loans fell. On the positive side were higher stock prices, lower bond yields, few business failures, and faster growth in M2. Before calculation of the four-week moving average, the index fell to 210.1, from 210.4. For the month of July, the index dropped sharply to 212.1, from 215.3 for June.

Leading index copyright 1991 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (8/10) thous. of net tons	1,588	1,625#	-16.2
AUTOS (8/10) units	90,746	76,465#	-23.8
TRUCKS (8/10) units	51,047	41,658#	-22.7
ELECTRIC POWER (8/10) millions of kilowatt-hours	64,086	63,847#	5.0
CRUDE-OIL REFINING (8/10) thous. of bbl./day	13,712	13,587#	-4.7
COAL (8/3) thous. of net tons	19,119#	20,036	-4.2
PAPERBOARD (8/3) thous. of tons	799.9#	807.2r	6.8
PAPER (8/3) thous. of tons	768.0#	752.0r	0.5
LUMBER (8/3) millions of ft.	523.8#	528.0	6.5
RAIL FREIGHT (8/3) billions of ton-miles	19.3#	19.6	-5.4

Sources: American Iron & Steel Institute, Ward's Automotive Reports, Edison Electric Institute, American Petroleum Institute, Energy Dept., American Paper Institute, WWPA, SFPA, Association of American Railroads

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (8/14)	137	136	148
GERMAN MARK (8/14)	1.74	1.71	1.55
BRITISH POUND (8/14)	1.69	1.71	1.91
FRENCH FRANC (8/14)	5.91	5.83	5.21
CANADIAN DOLLAR (8/14)	1.15	1.15	1.15
SWISS FRANC (8/14)	1.52	1.50	1.29
MEXICAN PESO (8/14)	3,029	3,024	2,886

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound expressed in pence.

PRICES

	Latest week	Week ago	% Change year ago
GOLD (8/14) \$/troy oz.	355.850	356.800	-10.7
STEEL SCRAP (8/13) #1 heavy, \$/ton	94.00	94.00	-20.3
FOODSTUFFS (8/12) index, 1967=100	203.0	205.2	-6.0
COPPER (8/10) c/lb.	106.4	105.1	-20.8
ALUMINUM (8/10) c/lb.	58.1	58.5	-28.3
WHEAT (8/10) #2 hard, \$/bu.	3.03	3.08	4.1
COTTON (8/10) strict low middling 1-1/16 in., c/lb.	69.17	69.12	-12.8

Sources: London Wednesday final setting, Chicago market, Commodity Research Bureau, Metals Week, Kansas City market, Memphis market

#Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1=Western Wood Products Assn. 2=Southern Forest Products Assn. 3=Free market value NA=Not available r=revised NM=Not meaningful

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (8/9) S&P 500	388.54	386.39	1.4
CORPORATE BOND YIELD, Aaa (8/9)	8.82%	8.93%	-6
INDUSTRIAL MATERIALS PRICES (8/9)	96.4	96.4	-8
BUSINESS FAILURES (8/2)	348	376	33
REAL ESTATE LOANS (7/31) billions	\$398.2	\$399.9r	4
MONEY SUPPLY, M2 (7/29) billions	\$3,410.2	\$3,396.2r	6
INITIAL CLAIMS, UNEMPLOYMENT (7/27) thous.	400	404	15

Sources: Standard & Poor's, Moody's, Journal of Commerce (index: 1980=100), Dun & Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. CIBC seasonal just data on business failures and real estate loans.

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
BUSINESS WEEK PRODUCTION INDEX (July)	176.0	176.5r	1
BUSINESS WEEK LEADING INDEX (July)	212.1	215.3r	5
CONSUMER PRICE INDEX (July)	136.2	136.0	5
PRODUCER PRICE INDEX (July) finished goods	121.1	121.4	6

Sources: BW CIBC BLS

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (7/29)	\$864.4	\$860.1r	6
BANKS' BUSINESS LOANS (7/31)	303.6	302.5r	-7
FREE RESERVES (8/7)	126	471r	-54
NONFINANCIAL COMMERCIAL PAPER (7/31)	144.3	145.0	-7

Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed for two-week period in millions)

MONEY MARKET RATES

	Latest week	Week ago	Year ago
FEDERAL FUNDS (8/13)	5.64%	5.70%	8.13
PRIME (8/14)	8.50	8.50	10.00
COMMERCIAL PAPER 3-MONTH (8/13)	5.70	5.84	7.85
CERTIFICATES OF DEPOSIT 3-MONTH (8/14)	5.63	5.64	7.94
EURODOLLAR 3-MONTH (8/10)	5.66	5.91	7.89

Sources: Federal Reserve Board, First Boston

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JAPANESE EDUCATION HAS SOME FAILINGS, TOO

The article "Time is not on America's side" (Economic Viewpoint, July 22), by Alan Blinder, makes a very good point about the differences between American and Japanese precollege students. Because of the fierce competition to get into Japanese colleges and universities, Japanese elementary and high school students must work astonishingly hard to gain admittance.

Certainly, when a Japanese high school student graduates, he or she is well ahead of the American student. However, when the Japanese student finishes high school and takes his or her competitive examinations to gain admittance to the best college or university possible, the competition is almost over. The Japanese view admittance to a college or university as the culmination of the educational process.

This is where the American college student starts to erase the education gap. American universities seem to be much more competitive than their Japanese counterparts. To wit, the large number of Japanese students attending American universities.

Our educational system in America is far from perfect. But the Japanese system also has some large faults. The graduate of an American university may not be as far behind his or her Japanese equivalent as Blinder implies.

Michael K. Smith
President
S&S Ltd.
Akron

THE GULF WAR'S ROLE IN ATTACKING THE COST OF CAPITAL

In your article "The U.S. has a new weapon: Low-cost capital" (Economics, July 29), the list of reasons for the turnaround in the U.S. cost of capital leaves out the most important factor.

Throughout the Eighties, to finance the budget and trade deficits we had to pay very high rates to attract the needed billions in foreign lending. These higher rates, of course, increased the cost of capital throughout the economy.

BUSINESS WEEK
AUGUST 26, 1991 *** 3228
ISSN 0007-7135

Published weekly, except for one issue in January by McGraw-Hill Inc. Founder James H. McGraw (1860-1948)
Executive, Editorial, Circulation, and Advertising Offices: McGraw-Hill Building, 1221 Avenue of the Americas, New York, N.Y. 10020
Telephone (212) 512-2000. Domestic Telex: 12-7560; International Telex: 232365, Cable: McGraw-Hill New York; TWX: 710-581-4879
U.S. subscription rate: \$44.95 per year, 2 years, \$74.95; 3 years, \$99.95. Single copies, \$2. Write for rates in other countries.
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The gulf war put a temporary halt to this. The combination of weapons sales to allies, contracts for rebuilding Iraq, and passing the hat among coalition partners (which, with the U.S. as major combatant, alone translated into the export of some \$40 billion worth of U.S. military services) all increased internal payments to the point where we need to attract foreign loans could be suspended. This enabled a timely and convenient reduction in rates to fight the recession and—among other things—reduce the cost of capital.

Your article is typical of the blind eye we cast on military involvement in the U.S. economy. In the case of an already collapsed Soviet Union, we can very clearly see the folly in this linkage (as Gorbachev pound missiles into place shares?).

Yet here at home, the military's economic role in foreign and domestic policies is entirely overlooked.

Frederick P. Jago
Cabot, Mass.

THE INCREDIBLE SHRINKING HOME EQUITY

Regarding the article "Even worse, less, consumers may spend more" (Economic Trends, July 29), economist Giulio Martini must be sipping cocktails with his statement "so home prices don't really affect economic growth."

Although "trading up" does appear to be a good idea during falling markets, all cash transactions, one's wealth seems to shrink when one applies this method to leveraged assets such as houses.

Say, for example, I own a \$100,000 house with \$20,000 of equity in it today, and I am eyeing a \$200,000 house in the next neighborhood. In a rising market, I wait for prices to rise 20%, my house has appreciated to \$120,000 and my equity is approximately \$40,000.

Although the other house has appreciated to \$240,000, my equity can purchase one-sixth (16.6%), maybe enough for the downpayment. But instead, let's say prices drop 20%. Now, I'm itching to move up to that presently priced \$160,000 house, but lo and behold, my house has depreciated to \$80,000 and my equity is a fat zero. I can now purchase

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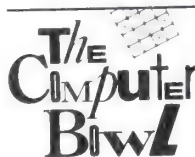
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Readers Report

ne of that other house with my pres-home equity.
Some prices do indeed affect econom-growth.

Robert W. May
West Hartford, Conn.

IF TAX BREAKS FOR SAVERS N'T BREED SAVINGS

Merrill Lynch's John Steffens, in his defense of tax incentives for peral savings ("Why Sammy can't e," Readers Report, July 22), neets two important considerations. st, the National Income & Product counts (NIPA), which measure aggre-e economic activity rather than con-ting selective surveys, indicate a sec-r trend downward in the household-ing ratio from 1980 to 1990, despite liberal tax benefits given IRAS in the ly to mid-1980s. In fact, the rate was hest in 1980 and 1981, before the lib-lization was initiated.
Second, since the incentives reduce tax enues and that in turn raises the dis-ings of the government, households uld have to increase their savings by least the amount of the average tax e in order to increase gross savings in

CORRECTIONS & CLARIFICATIONS

In the story "Batten down the hatches and rev up the Jacuzzis" (The Corpora-tion, Aug. 19), we incorrectly stated that Carnival Cruise Lines Inc. would go forward with a stock offering later this year. In fact, the offering took place on July 18.

the economy. The NIPA indicate that the ratio was not increased at all, much less by that amount. Whether the ratio would have fallen further without IRAS is conjectural.

The reality of saving is that it is more significant that the economy saves—not just households—particularly considering how small household sav-ings are in comparison with corporate cash flow.

In addition, the popularity of IRAS in the 1980s may indicate only that higher returns caused existing savers to seek those returns but did not turn nonsavers into savers.

Herbert M. Bernstein
Professor of Economics
Drexel University
Philadelphia

TRUMP: THEY DIDN'T REPOSSESS MY YACHT

Your article "Boston Co. learns all that glitters..." (Finance, July 22) incorrectly states that "Boston Co. has repossessed the Princess..." In fact, the Trump Princess was sold on a friendly basis to Boston Co. by me be-cause in the past year I was unable to find the time to use it. There was no repossession—a copy of the sale certi-ficate (price deleted) is enclosed—and there were no court cases or lawyers involved, other than those drawing up the documents. I was extremely happy with the sale, and hopefully, so were the talented representatives of Boston Co.

BUSINESS WEEK has inaccurately cov-ered Donald Trump for years. Few are coming out of the depression better—a story you surely would not like to write.

Donald J. Trump
New York

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THE NEW INDIVIDUALISTS: THE GENERATION AFTER THE ORGANIZATION MAN

By Paul Leinberger and Bruce Tucker
HarperCollins • 454pp • \$24.95

IS THE COMPANY MAN REALLY A GONER?

No phrase better captured the post-World War II business professional than *The Organization Man*—the title of a 1956 book by William H. Whyte Jr.

The Organization Man was a loyal, hard-working, white male who had given himself over entirely to his company. He avoided risk, wasn't terribly creative, and was quicker to take orders than to question authority. Whyte's controversial best-seller, along with C. Wright Mills's *White Collar* (1951) and Sloan Wilson's *The Man in the Gray Flannel Suit* (1955), helped shape an enduring stereotype of 1950s businessmen.

Paul Leinberger, a Palo Alto (Calif.) management consultant, knows that image well. He is the son of one of the men Whyte studied and the co-author of a new book that explores what became of the Organization Men and their families. With cooperation from Whyte, who turned over his notebooks, Leinberger and writer Bruce Tucker found and interviewed 175 of Whyte's original subjects. They then sought out the sons and daughters of these men, to compare the two generations' views of their careers.

What a great idea! In another 20 years, the baby-boomers will dominate the ranks of American chief executives. What makes them tick and how growing up as children of Organization Men shaped some of them are subjects worthy of extensive examination.

But *The New Individualists* is a disappointment. This undisciplined book sorely needed an aggressive editor. At times, the text descends into sociobabble: "The notion of artificial persons sounds repugnant, robotic and conformist. But consider how the ideology of authenticity permits a far more thorough domination of individuals than does the frank acknowledgement of artificiality." The authors cite, quote, and comment on virtually every important demographic, sociological, or psychological study of the past half-century. And

in defining the New Individualists, they often seem to be overreaching.

Yet parts of the book are fascinating—especially the well-drawn portraits of two families, the Myerses and the Harrisons. Ray Myers, 71, is former general counsel of Continental Illinois National Bank & Trust Co. Dave Harrison, 73, was an executive at General Motors Corp. Both were highly successful, working for decades in one organization. Says Harrison's wife, Helen: "We had always done what General Motors told us to do." That included moving a dozen

were before," he wrote. "The people who staff them are pretty much the same as those who did before."

The evidence is on Whyte's side. Every year, most newly minted MBAs seek jobs with large, brand-name corporations. In city bars, some young people now greet each other not by their names but by the names of the companies they work for ("Hey, Merrill," shouts one V. Streeter to another.)

Of course, there have been changes in the management profession since the '50s—the most obvious being the emergence of women and the growing all of entrepreneurialism. But most Americans still yearn to belong to organizations and would gladly trade their loyalty for security, just as their fathers. If loyalty isn't what it used to be, primarily because in this fast-changing world, organizations have found it difficult to remain loyal to employees. To stay competitive, many companies have

had to lay people off, cut benefits, or slow down salary increases.

One of the most troubling aspects of *The New Individualists* is that it perpetuates a negative distortion of Whyte's work. The Organization Man, Leinberger and Tucker contend, was a great follower and a poor leader who "neither used creativity nor was ever accused of possessing it." This view degrades the achievement of the managers who built America into the economic force it became during the postwar period. Much

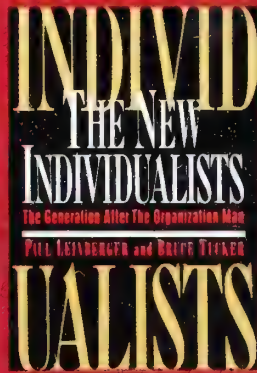
risk-taking and innovation went into that triumph, just as much managerial neglect has contributed to the subsequent decline in our competitiveness.

And what do Leinberger and Tucker say of the new generation? They are "poor followers and poor leaders... the function best in solitary situations, and when they find themselves in organizations, they tend to behave in ways that are purely self-interested, whether single-mindedly pursuing their careers or by reserving their best energies for private life..." In other words, some do this, and some do that. It's hard to generalize about the baby-boomers. But it's a safe bet that, 40 years from now, many observers will be using the expression the New Individualists to define the generation that's currently coming to power.

BY JOHN A. BYRNE

Senior Writer Byrne covers management

T rue, loyalty isn't what it used to be. But managers haven't changed all that much since the Fifties



times in 38 years with the company.

The children of both families are pursuing diverse careers. Of the Myerses' three sons, for example, one is a Mellon Bank vice-president, another worked nearly 10 years for Memorex Corp. before starting his own Silicon Valley software venture, and a third is a carpenter in Colorado. This range of vocations doesn't seem remarkable. What makes the portraits satisfying are the candid reflections of parents and children on their personal and professional lives.

Unfortunately, the authors have tried too hard to formulate a theory from the diversity they see in the next generation. Their thesis—that the Organization Man has given way to the New Individualist—isn't very persuasive. In 1986, in fact, Whyte published a critique of their early findings. "The United States continues to be dominated by large organizations, and they are run much as they

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ILLEGAL IMMIGRATION: WOULD A NATIONAL ID CARD HELP?

BY ROBERT KUTTNER



Immigration reform hasn't stopped the wave of undocumented workers. A simple system of identification might curb the hiring of illegal aliens—and prevent billions of dollars in wages from leaving the U.S.

Peek into any U.S. hotel or restaurant kitchen, and you are likely to spy foreigners without green cards through the dishwasher steam. These workers are known as "illegal aliens" or more benignly as "undocumented workers," depending on your view of the issue. Foreigners unauthorized to work in the U.S. can also be found in garment factories, tomato fields, parking garages, taxicabs, behind a broom, and performing a host of other tasks whose common features are long hours, scut work, and low pay. Millions of such workers continue to flood the labor force, despite a long-fought 1986 immigration-reform law that liberalized legal immigration in exchange for what was supposed to be a crackdown on unlawful entry and employment.

The novel idea of the 1986 law was to hold businesses accountable for hiring improperly documented workers. But the law had to be watered down to win enactment because of opposition from employers, who justifiably resisted being deputized as border guards, and from civil rights groups with legitimate fears that anyone with a Hispanic surname or Asian features might be subjected to the third degree. In practice, an employer need only make a reasonable effort to examine a worker's documents—a Social Security card will usually do—and the employer is legally off the hook. But of course, such documents are notoriously easy to forge or misuse.

LONG HOURS. In the real world, according to a source in the restaurant industry, the system works like this: An unauthorized immigrant job applicant produces either a borrowed Social Security card or a forged one. Other corroborating fake IDs are even easier to get. The worker then claims a very large family—so many that no withholding is taken out of his or her paycheck. My source says he doesn't know—or care—which of his employees are working under their own names, which ones are citizens, or which ones are aliens. What he does know, he says, is that they are all hard workers. Many of them work the breakfast shift at one restaurant, the day shift at another, and even dinner at a third. Living collectively and working a 14- or 16-hour day, they can make close to \$1,000 a week, effectively tax-free except for deductions for FICA (Federal Insurance Contribution Act). Most of their earnings are sent home to El Salvador or Colombia. Or Nigeria, or Ireland, or China, or Haiti, or Mexico, or wherever.

What are we to make of this? In a sense, there is a crude social bargain here. The unauthorized workers enjoy the benefits of U.S. residence without paying U.S. income tax. U.S. consumers and employers get the bene-

fits of these hard-working foreigners, whose wages—though low—are infinitely greater than they could earn in their homelands.

On the other hand, foreigners receive benefits from payroll deductions credited to bogus Social Security numbers. Also, billions of dollars worth of wages are sent out of the economy, rather than going to purchase goods and services here. And hard-won benefits for American workers—minimum wage, the eight-hour day, pensions—are undermined by an enormous underground economy.

AMBIVALENCE. Recently, the Immigration and Naturalization Service announced the latest in a series of futile crackdowns. In the past four months, approximately \$3.2 million in fines have been imposed on employers for hiring obvious illegals. But that's about a dollar for each of the estimated 2 million to 4 million foreigners working illegally in the U.S. In the entire country, the INS has only about 1,800 special agents working in nonborder areas, with several hundred of them devoting their time to other matters, such as smuggling or fake marriages.

The deeper problem, I suspect, is a profound public ambivalence about the entire question. With the exception of native Americans, we are a nation of immigrants. Some of our parents and grandparents sneaked into this country and went on not only to thrive but to give a good deal back. In the 1960s, when liberals were indignant about illegal immigrant workers, conservatives responded that such workers were more of an asset than a drain on the economy. That debate continues. Some have even argued that our borders should simply be thrown open.

Moreover, Americans also have a pathological distrust of government identification cards. Until recently, Social Security cards included the utterly disingenuous disclaimer: "For Social Security and tax purposes—not for identification," even though Social Security numbers are now in standard use for driver's licenses, bank accounts, insurance policies, passport applications, and so on.

If America were more adult about this issue, like some Western European nations, we might save ourselves endless inconvenience by establishing a single official ID. Employees could ask to see it, and counterfeiting it would be a serious crime.

That way, Americans might finally decide just what sort of immigration policy they really want and have that policy enforced. The current situation, while randomly helping a number of lucky individual migrant workers, has the corrosive side effect of eroding the rule of law.

ROBERT KUTTNER IS ECONOMICS
VICE PRESIDENT FOR THE NEW
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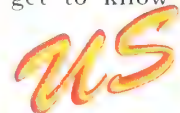


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BY GENE KORETZ

A WORLDWIDE CREDIT CRUNCH MAY BE FLASHING A RED ALERT

The Federal Reserve's latest easing came in response to fears stirred by stagnant money growth in the context of a sluggish recovery. But as economist Bluford Putnam of London's Kleinwort Benson Securities Ltd. notes in a recent analysis, depressed monetary growth is more than a U.S. phenomenon. "Money stock around the world," he says, "is growing at an historically slow pace, suggesting to monetarists a severe danger of world recession unfolding in the coming 12 months."

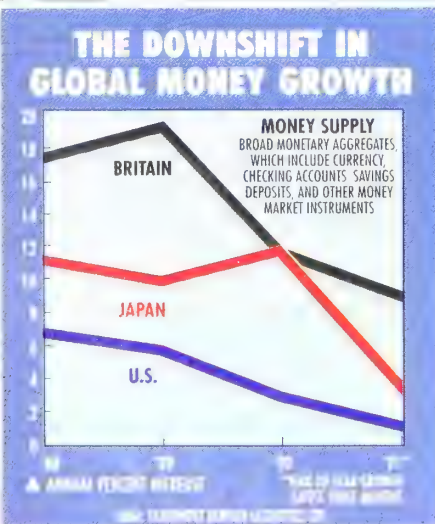
This slowdown is apparent both in the narrow definitions of money, which focus on cash and checking accounts, and in broader measures, which include savings

may be developing. For another, tight monetary policies have had a strong impact in countries such as Britain, Australia, New Zealand, and Canada—producing severe recessions while making significant strides in quelling inflation.

Such progress on the inflation front is welcome. But the big question is whether monetary authorities are yet aware of the degree of monetary stimulus needed to assure future economic expansion.

Putnam notes that U.S. banks weren't the only institutions hurt by the debt excesses of the 1980s. And they aren't alone in adopting new conservative lending policies to bolster their credit standings. In his view, the continuing slow growth of the broad monetary measures around the world reflects the retrenchment of national banking systems, which is tending to restrain credit expansion and undermine economic growth.

In sum, the bank credit crunch may be a global phenomenon, and it may require aggressive easing by foreign monetary authorities, as well as the Fed, to avert a continuing world economic slowdown. To central banks, says Putnam, the sluggish behavior of the broad money supply "should be an especially loud warning."



accounts and other less liquid money-market instruments. And it affects such industrial nations as Japan, Britain, France, Switzerland, Canada, Australia, and New Zealand, as well as the U.S.

Just how worrisome is the money slump? Putnam notes that predictable links between money growth and such variables as inflation and economic activity seemed to break down in the 1980s, allowing many central banks to ignore their own targets. A major cause of this breakdown, he says, was the deregulation of world banking systems, which changed the nature of monetary measures in unpredictable ways.

But now money growth is receiving renewed attention. For one thing, global bank deregulation has now largely ended, suggesting that new stable relationships between the monetary aggregates and inflation and economic activity

PROFIT MARGINS: A PLEASANT SURPRISE COULD BE IN STORE

If the recovery picks up some steam, profit margins could widen appreciably, says economist Susan Lakatos of Kidder, Peabody & Co. Lakatos points out that service-sector productivity last quarter posted its first year-over-year gain since 1988. As a result of this development, which reflects employment cutbacks that began late last year, unit labor costs in the nonmanufacturing sector, compared with their year-earlier level, were up less than service prices for the first time since 1989. So, profit margins in service industries actually widened slightly.

Meanwhile, notes Lakatos, manufacturers are sitting in the catbird seat. Having slashed payrolls for two years, they managed to keep increases in unit labor costs below their price hikes throughout the past recession—the first recession ever in which manufacturing profit margins didn't get squeezed.

That record, says Lakatos, "implies that manufacturers have an unprecedented opportunity to benefit from volume gains as the recovery accelerates." And signs that the service sector may finally be getting its own labor-cost problems under control suggest that its profits could get a nice boost, as well.

WILL EASIER MONEY IN JAPAN COME JUST IN TIME FOR BUSH?

The prospect of interest-rate cuts abroad over the coming year spurs good news for the Bush Administration, contends economist David Hale of Kiper Financial Services Inc. In particular, he notes that the Japanese stock market crash of 1990-91 and related problems in the banking system erupted at a tumultuous time for the Republicans, since they forced the Japanese to tighten money in the middle rather than at the end of the U.S. Presidential term.

Japan's central bank, he says, has not successfully slowed the economy and has taken the back of the speculative surge in stock and land values that destabilized the Tokyo stock market. Thus, suggests Hale, "Japan will be in a position to lower interest rates significantly during the runup to the 1992 Presidential election in the U.S."—a policy that should bolster U.S. economic growth.

Japanese monetary policy has worked to the advantage of the White House before. In 1987 and 1988, Hale notes, "Japan kept interest rates artificially low to help stabilize the dollar and lessen the risk of a recessionary hard landing in the U.S."

AN ECONOMIST PONDERES HOW FAST OLD MEN SLOW DOWN

Joggers, take note. In a recent National Bureau of Economic Research working paper, Yale University economist Ray Fair seeks to answer the question "How fast do old men slow down?"

Using econometric techniques, Fair analyzes data on men's track and field records by age. For most of the running events (400 meters to a half marathon), he finds that the slowdown rate averages about 0.8% a year between the ages of 35 and 51, and then increases to about 1% a year by age 60, 1.5% by age 75, and 2% by age 95. The slowdown rate is smaller for shorter distances and larger for field events such as the shot put and discus throw.

Why should all this concern an economist? Fair is struck by how small the slowdown rates are. Perhaps, he muses, they have something to tell about productivity loss with age. "Of course," he adds, "the numbers are of interest to old runners as they run ever more slowly into the sunset."



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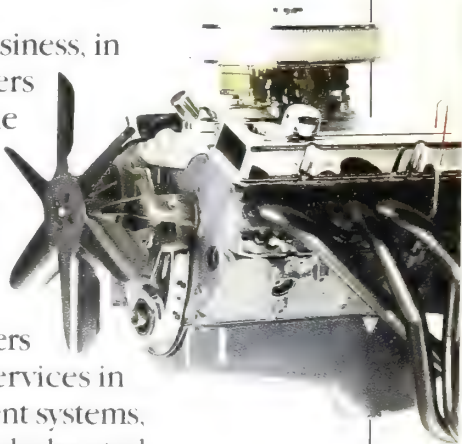


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BROADWAY'S LONGEST-RUNNING FLOP

It was high noon—or just about—in Columbus Circle. I watched as some 35 squatters awaited the deadline to leave their recent residences in front of the New York Coliseum. Complaints about the homeless people who were overrunning the sidewalk had led to an eviction order.

Police cordoned off the area, and, muttering curses, the squatters carted their belongings away. After the cops and reporters left, the circle settled down again. It probably hadn't seen so much press since Mafia boss Joe Columbo was wounded there in 1971 at an Italian-American Unity Day rally. I was only a year old then, but I remember grown-ups for years rehashing the shooting and the prompt killing of the would-be hit man, who had lived near us.

Not much goes on here, yet everything goes on here. Intended to echo the grand hubs of European capitals, Columbus Circle is really a triangle, and a somewhat dysfunctional one at that. Its flow is interrupted by traffic lights, weirdly angled intersections, and a parking lot at its very heart. Buses pass through on their way uptown and downtown and from midtown to upstate. Three major subway lines roar below. Horse-drawn carriages line up to take tourists through nearby Central Park, while New Yorkers bustle through on their way to somewhere else.

DREAMS DEFERRED. I wondered about these crossroads and thought, surely Columbus Circle must have been meant for something else, something greater. And, true enough, I learned that the circle has always been a promising but neglected stepchild, looking on while the city grew up around it. Time after time, as the city's economy boomed, grand plans were laid for the circle. But they all had a way of turning into hard-luck stories—nagging reminders that New York isn't always the city of unlimited opportunity.

Perched some 70 feet above the traffic and watching all the deferred dreams pass is the granite statue of Christopher Columbus, a gift from Italian immigrants in 1892 to mark the quadricenten-

nial of Columbus' landing in the New World. Ninth Avenue became Columbus Avenue as part of an effort to bring prestige and value to the blocks surrounding the new circle.

It was William Randolph Hearst's twin obsessions, money and his mistress, actress Marion Davies, that drew him to the area. In 1912, the tycoon publisher began upgrading the district by furnish-



PHOTO OP: CITY RESIDENTS JUST HURRY THROUGH THE CIRCLE

ing the Maine Memorial at the entrance to Central Park. The sculpture commemorates the sinking of the U.S. battleship Maine, an event that triggered the Spanish-American War, which Hearst's jingoistic tabloids had promoted. Later, he bought and renovated the Cosmopolitan Theater on 58th Street as a showplace for Davies, who, alas, never quite became the star Hearst had in mind.

In the 1920s, hearing talk of plans for

Occasionally, parts of the shuttered Coliseum are rented for such events as *American Gladiators* tryouts

a Hudson River bridge at 59th Street. Hearst bought more property around Columbus Circle. But the span to New Jersey, the George Washington Bridge, was built 120 blocks north in 1931.

In a final attempt to make Columbus Circle a magnet to rival Madison Square and Times Square, Hearst planned his International Magazine Building tower over 57th Street. But the Depression helped create one of New York's true architectural oddities instead: a six-story building with huge sandstone columns on each corner that had been scaled to decorate a massive skyscraper.

Development around the circle was dormant until the 1950s, when *West Side Story* was on everyone's mind and urban renewal was the order of the day.

Along with the tenement razings that cleared the site for Lincoln Center to the north, planning czar Robert Moses commissioned the New York Coliseum. In its heyday, the Coliseum's four exhibition floors hosted everything from a Soviet cultural exposition to a political rally for John F. Kennedy and drew 24 million visitors in 10 years.

Even so, the facility was deemed too small for conventions that were growing ever larger. So, in 1986, the city opened the Jacob K. Javits Convention Center between 34th and 37th streets, and the days, the Coliseum's floors seldom had anything but dust and plywood. Occasionally, portions are rented for such events as tryouts for TV's semibarbaric *American Gladiators* and registration for the New York City Marathon.

To the skeleton crew that stays on

Coliseum, the Javits Center is un-
 shakable—when it has to be mentioned,
 “that place over there.” Arthur Zer-
 mer, who began at the Coliseum 35 years
 ago as an air-conditioning repairman,
 tells me that “I hear it’s sinking, even.”
 That won’t save the Coliseum. Pub-
 lisher/developer Mortimer Zuckerman
 agreed to buy the Coliseum in 1985. In
 place, he planned two 68-story office
 towers that, critics calculated, would
 cast a shadow over much of Central
 Park. Jacqueline Onassis, Bill Moyers,
 and other prominent New Yorkers
 waged an epic battle to scale back the
 project. On his third try, Zuckerman
 came up with a 59-story plan that was
 accepted by all parties involved.
 Plans remain in limbo, though. Zucker-
 man must prove that the Clean Air Act
 can’t be violated, since the Coliseum is
 covered with asbestos that is harmless as
 long as it is contained. Even if Zucker-
 man gets demolition approval, however,
 Manhattan has a glut of unused offices
 that probably will last for some time.

WHITE ELEPHANT. A quarter-turn to the
 northeast on the circle lies another mon-
 ument to broken dreams—in this case,
 the house of Huntington Hartford, heir to
 the A&P fortune. In 1957, he commis-
 sioned Edward Durrell Stone to design
 the Huntington Hartford Gallery of
 Modern Art. The result, a toy-like mar-
 ble building that reflects Stone’s inter-
 pretation of Middle Eastern motifs, was
 opened in 1964 with exhibitions of the
 works of Salvador Dali and José Clemen-
 te Orozco. But Hartford never came
 close to his dream of upstaging the Mu-
 seum of Modern Art and closed the gal-
 lery in 1969. Nearly windowless, the
 building was unrentable as office space.
 Finally, Gulf & Western Inc. (now Para-
 mount Communications Inc.), another
 circle resident, bought it and donated it
 to the city for use as a visitors’ bureau.
 Returning to the circle a month after
 the expulsion of the homeless, I see that
 while some things have changed, much
 remains really still the same. The vast side-
 walk in front of the Coliseum now fea-
 res fast-food stands and lunching hard-
 hats, who are tearing up the nearby
 pavement. Many of the displaced squat-
 ters have merely moved across the circle
 to the fringes of Central Park, where
 they hang out in relative peace, barring
 the odd thunderstorm or turf squabble.
 I can’t help but feel that the circle—
 a childhood that it is to nearby Carnegie
 Hall, Broadway, and any number of
 Manhattan landmarks—will be forever
 struggling to find an identity of its own
 under the never-faltering gaze of Chris-
 topher Columbus, that confused but
 helpful navigator.

HEATHER KEETS

*Heather Keets grew up an hour away
 from Columbus Circle in New Jersey.*



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IF IT'S A RECOVERY, IT SURE DOESN'T FEEL LIKE ONE

Most economists believe the recession ended three or four months ago. But an ABC News poll of 1,200 Americans taken in late July revealed that 85% of them thought the economy was still headed downhill. The Conference Board says consumer confidence has gone nowhere since the end of the war. And the U.S. Chamber of Commerce reports that business confidence is down in the dumps as well. To the public, it just doesn't feel like a recovery.



The sector where all this is hitting especially hard is services. As weak demand and prices batter many labor-intensive service industries, cost-cutting is becoming a priority. Goods producers bit the bullet in the 1980s, when competition forced downsizings and productivity gains, in order to enhance profitability. Now, a major restructuring is taking place in services.

SERVICE JOBS ARE STILL IN THE TANK

This is a big reason why the recovery doesn't feel so good. Service industries employ three-fourths of all workers, and that means plenty of consumers are more than a little worried about their jobs—and rightfully so. During the recession—from the third quarter of 1990 to the second quarter of 1991—private service jobs fell at an annual rate of 0.6%, one of the sharpest contractions in the postwar era (chart). Service output, however, didn't slow at all during the downturn. Real gross national product in private services grew at an annual rate of 3%, the same pace as in the year preceding the recession. In the past, it took a sharp slowdown in service output to produce such a steep slide in employment. Such a wide disparity this time around clearly reflects an effort to cut costs, improve productivity, and shore up profit margins. And it suggests that the current round of cost-cutting is more structural than cyclical. One reason is that the squeeze on profit margins in service businesses is not letting up. Service-industry margins stood at 7.1% of service GNP in the first quar-

ter. This margin is little changed from 1990, and it has been shrinking since hitting 9.6% in 1986. Initial reports on second-quarter profits suggest no improvement.

With pricing power limited by slow inflation, profit margins will not improve substantially until service productivity picks up enough to offset the cost of labor. That will allow the pace of unit labor costs to ease back in relation to prices, thus making more room for earnings. The slowdown in service wages that has already begun, combined with low job growth, means the outlook for service companies will improve in the long haul.

Productivity always picks up in a recovery, as output outpaces employment. But the gains in service efficiency now developing appear to be more than just cyclical. Service employment began to slow down two years ago, well before the recession began, and there is no evidence that hiring will pick up any time soon.

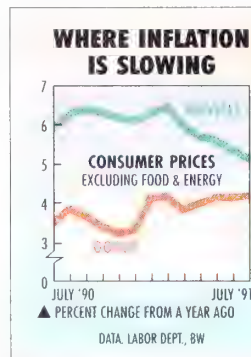
Indeed, the Conference Board's index of help-wanted advertising ticked up in June, but it has been nearly flat since February. The American Management Assn.'s survey of corporate layoffs for the year ended in June showed the most widespread cuts since the survey began in 1987. And the National Federation of Independent Business says that the hiring plans of small businesses fell last quarter.

The upside of all this is a brighter outlook for inflation, since service prices had been the last bastion of price strength. The downside is that employment is not likely to grow any faster than the labor force in coming months. That means the jobless rate could be stuck at about 7% well into 1992. For consumers, who must lead a recovery, that's not much to feel good about.

THE FIRE UNDER PRICES IS FLICKERING

The inflation outlook is more comforting, however. The consumer price index rose a modest 0.2% in July, in line with the increases in the previous three months. Yearly consumer inflation fell to 4.4% last month, after peaking at 6.4% in October. Slower growth in service prices has led the improvement (chart).

Some of that decline reflects the gulf war's impact on energy prices. But even excluding food and energy, the core rate of inflation is also coming down. The core CPI rose a faster 0.4% in July, but yearly core inflation fell to 4.8%, after hitting 5.7% in February. Again, services led



Business Outlook

the way. Inflation in nonenergy services declined to 5.1% in July, from 6.5% in February.

Somewhat surprisingly, core inflation in goods prices has been more stubborn. Excluding food and energy, the CPI for goods in July rose 4.2% from last year, faster than the 3.5% pace in the previous year. That's a bit odd, given weak commodity prices, tame producer prices for finished goods, and excess capacity in manufacturing.

One explanation is higher taxes on goods such as gasoline and tobacco, along with sales-tax hikes in many states. But those effects will be temporary. The inflation fundamentals for goods are much more favorable than those for services, since price hikes for services such as medical care and education will be harder to rein in.

Indeed, the producer price index for finished goods fell 0.2% in July, reflecting lower costs for food and energy. Still, the core PPI rose only 0.2% and has increased 3.3% during the past year, the slowest annual pace in three years. Prices at the earlier stages of production are either barely rising or falling. Such weak pricing suggests that profit margins in manufacturing are still under as much pressure as those in services.

SHOPPERS ARE IN NO RUSH TO BUY

Retailing is a perfect example of an industry caught between weak consumer demand and the service sector's profit-and-productivity squeeze. True, shoppers have returned to the malls, but they have yet to boost their spending in any significant or sustained way.

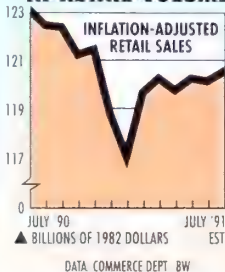
To compensate for sluggish demand, the retail industry—the second-largest category in service employment—is likely to close more stores and pare payrolls further in an effort to enhance the bottom line.

In July, retail sales increased by 0.5%, to \$153.7 billion. While the gain was a bit larger than expected, it is far below the increases recorded during the early stages of previous recoveries. And after adjusting for inflation, real volume remains 2% below its year-ago level (chart).

With sales still sluggish at best, retailers have been selling from their inventories, as opposed to placing new orders. Retail inventories fell 0.2% in June, and they have declined in seven of the last eight months.

Other industries also continue to cut their stock levels. Inventories held by manufacturers, wholesalers, and retailers fell 0.3% in June, and the May decline was revised to show a drop of 0.6%, instead of 0.5%. Since inventory liquidation last quarter was steeper than the Commerce Dept.'s initial reading, the slim 0.4% increase in second-quarter GNP could be revised down.

NOT MUCH RECOVERY IN RETAIL VOLUME



A pickup in car-buying has kept auto inventories low. Car sales rose by a strong 1.1% last month, the third consecutive gain. But domestically made cars performed poorly in early August, selling at a 6.2 million annual rate, down from 6.8 million for all of July.

Excluding autos, retail sales rose a modest 0.3% in July, with furniture and department stores

posting healthy advances. Purchases of building materials, however, fell for the third month in a row.

Real retail purchases started this quarter slightly ahead of their second-quarter average, but maintaining that lead will be difficult. Household finances look shaky right now, because of the weakness in service hiring and smaller wage gains generally.

In addition, consumers are staggering under an \$8 billion hike in state taxes this year, the largest in 20 years, according to the National Conference of State Legislatures. That will erode purchasing power further.

Economists may trumpet the recovery, but in the face of sluggish demand, sagging profits, more layoffs, and higher taxes, it's no wonder that consumers and businesses disagree.

THE WEEK AHEAD

FEDERAL BUDGET

Wednesday, Aug. 21, 2 p.m.

The U.S. government will probably post a deficit of \$38.1 billion for July, according to economists surveyed by MMS International, a unit of McGraw-Hill Inc. That gap would be much larger than the \$25.9 billion red-ink total of July, 1990. Slower tax receipts—a casualty of the recession—are widening the federal deficit. The White House estimates that the deficit will hit a record \$282 billion in fiscal 1991, which ends on Sept. 30.

INITIAL UNEMPLOYMENT CLAIMS

Thursday, Aug. 22, 8:30 a.m.

New filings for state unemployment insurance benefits are likely to stand at an

annual rate of about 400,000 for the week ended Aug. 10, the same level as at the end of July. Claims peaked in March and have come down by almost 140,000 since then, as the economy struggles to recover. In recent weeks, claims have risen because some auto workers have been laid off temporarily, as factories switch over to new models.

DURABLE GOODS ORDERS

Friday, Aug. 23, 8:30 a.m.

New orders placed with durable goods manufacturers likely rose by 1.3% in July, says the MMS consensus. That's suggested by the pickup in auto production and by a positive reading in the July order index compiled by the National Association of Purchasing Management.

The expected gain would reverse the 1.4% decline in orders in June. Even so, the backlog of unfilled orders probably dropped in July, the sixth consecutive drawdown in unfilled demand. In July the backlog slid by 1.1%.

CAR SALES

Friday, Aug. 23, 5 p.m.

New domestically made cars likely sold at an annual rate of about 6.5 million during the middle 10 days of August. This pace is a bit better than the 6 million pace of early August. In July U.S.-made cars sold at a respectable 6 million rate—the highest pace since October. Some consumers may buy in August to beat the price increases announced for many 1992 car models.

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MOM, WHAT'S INFLATION?

FROM CARS TO HAIRDOS, THE LID IS ON PRICES

The fever has broken.

For some 20 years, the U.S. economy has been afflicted by a seemingly incurable case of inflation. Since 1973, core inflation—the increase in all consumer prices except food and energy—has spiraled up by 4% or more each and every year. Even the savage recession of 1981-82 couldn't drag inflation below this level. For an entire generation of Americans, persistent inflation is all they've ever known.

Get ready for a change. Since February, 1991, core inflation is running at an annual rate of only 3.1%, according to the latest government figures (charts). That's down from 5.2% in 1990. Inflation next year, most forecasters say, will run between 3.5% and 3.8%. "Core inflation is drifting down, and we've broken the 4% barrier," observes Donald Ratajczak, an economist at Georgia State University and a leading price watcher.

The inflation slowdown could last well into the 1990s. The key reason for optimism: Service-sector inflation, troublesome for most of the past decade, at last appears to be moderating. In part, that's because the recent recession forced a wide range of service businesses, from restaurants to apartment buildings to hair styling, to hold down prices. But even as the economy starts to recover, banks, insurers, ad agencies, and others are being forced to become more competitive by cutting costs and laying off workers with a vengeance. This promises to boost productivity, lower costs, and lessen the need to increase prices. As a result, says Morgan Stanley & Co. senior economist Stephen S. Roach, "we could be moving into an era of 3%-to-3.5% inflation."

WISHFUL THINKING? True, not everyone believes these gains will be lasting. The bond market, for instance, is still worried about prices surging after the economy begins to recover in earnest. "The collective memory is a world of high inflation and a tendency for it to accelerate," notes David Resler, senior vice-president at Nomura Securities Inter-

national Inc. Bond traders "can't remember times when inflation was 2% to 3%," says Resler. Until the bond market is convinced that inflation has been dampened for the foreseeable future, real interest rates will remain high.

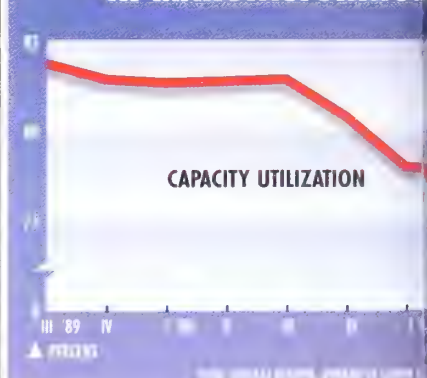
Low inflation is no stranger to manufacturers. At the high-tech end, computer prices have been on the wane for years, squeezing the industry while benefiting consumers. Over the past year, for example, personal computer prices have dropped by 8.2%, according to Store Board, a firm that tracks sales of personal computers sold through computer stores. Prices for some basic products are falling as well. Steel prices are now at their lowest level in 10 years, and so is the price of wallboard, reports USG Corp., the big Chicago-based building-supplies company.

Or take the auto industry. While sticker prices on new cars have roughly paralleled the consumer price index since 1981, the actual transaction prices in recent years have lagged far behind. Since 1988, for example, the price paid by car buyers has risen at an annual rate of only 2.1%, far less than the overall inflation rate of 4.9%. And while auto makers, such as General Motors Corp., have announced 3% price increases for their 1992 models, that's more hope than reality. "These prices won't stick," says Wertheim Schroder & Co. analyst John Casesa. "We now have 42 nameplates competing in the most competitive market in the world in the middle of a recession. It's impossible to pass along a meaningful price increase in this environment."

For the first time in years, service businesses are tasting the price pressures that have wracked manufacturers. Take housing, which makes up more than 40% of the CPI. Over the past three months, housing costs have risen at an annual rate of only 2.1%. No one expects a quick recovery in prices, given the severe slump in the housing market. Look around Boston. There, two-bedroom apartments that once rented at \$1,200 to



THERE'S PLENTY OF SLACK IN MANUFACTURING.



\$1,300 a month are now going for a little as \$795. "Rents have declined 10% to 30%," says Michael Polacco, president of Boston-based Popular Properties Realty Inc.

Medical care is another service that consumers must dig deep in their pockets to buy. Years of effort by the government and private insurers to slow inflation of health care prices finally

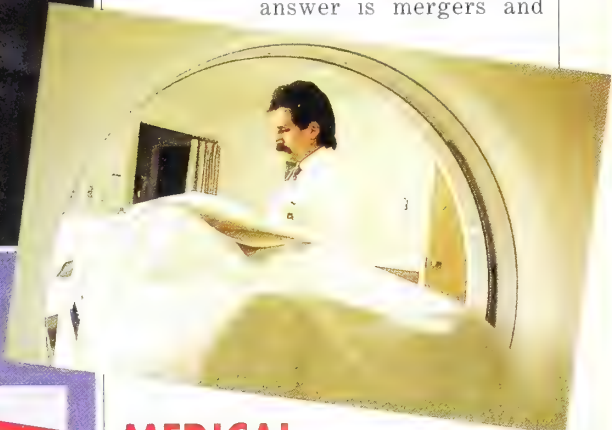


HOUSING SHOWING A PROSPECTIVE TENANT A MARYLAND APARTMENT: RENTS ARE DOWN, AND HOME PRICES AREN'T LIKELY TO PERK UP SOON

In a chain reaction, businesses that are having trouble raising prices are forcing their suppliers to hold down prices as well. At Michela's, a Cambridge (Mass.) restaurant, General Manager Christopher Myers renegotiated contracts for linen, floor maintenance, and cleaning supplies. The one supplier that refused to budge was replaced earlier this year. The result? "We probably cut our product costs for dishwashing and all the products we use around the restaurant by 35%," says Myers.

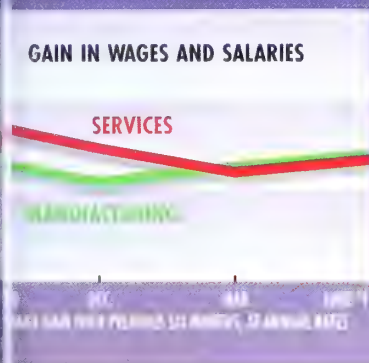
Nor will corporations pay top dollar for legal services anymore. "Over the past two years, we have seen law firms being more willing to enter into agreements with lower rates," says Jed Ringel, president of Law Audit Services, a New York-based legal billing consultant firm. Even after the recession is over, says Ringel, the pressure on fees will continue. "The myth has been broken that this is not a business."

The main force holding down service-sector inflation over the long run will be the need to stay in business. Right now, there are too many banks, retail stores, and office buildings. In some cases, the answer is mergers and

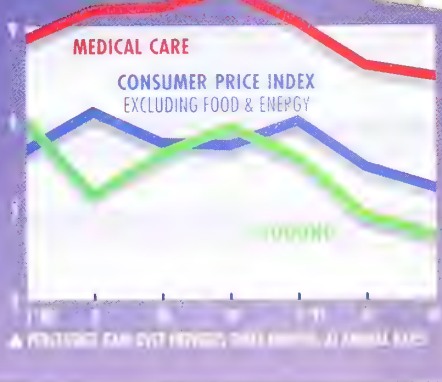


MEDICAL COSTS A CAT SCANNER: THE BATTLE AGAINST SOARING BILLS MAY FINALLY BE PAYING OFF

AND EVEN IN SERVICES, WAGES ARE MODERATING...



...DAMPENING RATES OF INFLATION



ms to be having some effect. Over the past three months, the inflation rate for medical care has run at about 7.3%. That's high, but it's less than the 10.2% recorded just nine months ago. Moreover, the price of X-ray machines and other sophisticated medical equipment has risen only 1.9% over the past year, the government reports. On a smaller scale, this goes for per-

sonal services, too. The cost of hiring someone to do home repairs has risen at an annual rate of just 1.6% this year. At Jeannie's Hair Design, a San Francisco neighborhood business, the price of a basic haircut usually goes up \$1 a year, reports owner Jeannie Mock. But not this year. "I just didn't do it," she says. "My rent hasn't been raised. I didn't need to increase my prices."

consolidations. The three recently announced megabank mergers (page 24) will cost at least 26,000 jobs as the merged companies eliminate overlapping operations.

RUDE SHOCK. Hard as it will be on those who get pink slips, these cuts will improve the inflation outlook twofold. First, added unemployment will hold down wages. And with fewer hands doing more, productivity will jump. Morgan Stanley calculates that nonmanufacturing productivity rose by 1.3% in the second quarter. That's a staggering achievement next to the last two recessions, when it fell sharply. "Bittersweet consolation to the white-collar workers who are the victims of restructuring," says Morgan Stanley's Roach, "but

that's really good news for inflation."

It's not just workers pounding the pavements who lose from low inflation. Elderly people living on interest income also suffer. Interest rates on certificates of deposit sank from 8% to 6% in the last year. And anybody who bought real estate expecting higher or even stable prices has had a rude shock.

But lower interest rates will spur all

types of capital investment. And many debt-laden companies will see immediate gains. At New York-based Avon Products Inc., for example, the rate on 70% of its short-term debt floats, so any general drop in rates is an immediate boon.

The full benefits of lower inflation won't come right away. It'll take "six to nine months of recovery without inflation," says Ratajczak, to convince people

that low inflation is here to stay. The capital markets should catch on, lowering interest rates. And that's why important headway that's been made service-sector inflation, if it turns out to be more than fleeting, offers real promise of brighter times to come.

By Michael J. Mandel in New York, and David Woodruff in Detroit, Gary Williams in Boston, and bureau report

GLOOM IN THE FIELDS, SMILES IN THE SUPERMARKET

Across Harold McQueen's parched 1,100 acres of corn in central Illinois, the winds of early August were very nearly the last straw. Hot and dry, they blew for a week straight, sucking the life out of his crops. Down the road, a neighbor parked his combine and tracted into his fields to plow under his worthless corn crop. But not McQueen—not yet.

Good for him. Across the Midwest, four days of rains followed those dry winds, salvaging some corn and saving soybean crops from Minnesota through Iowa and across to Indiana. "Droughts end a lot faster than they start," cheered Daniel Basse, director of research for AgResource of Chicago. "There is no drought of 1991."

The U.S. Agriculture Dept. on Aug. 12 underlined the point by forecasting that harvests, while below last year's levels, still figure to be healthy (chart). Combine that with a decline in agricultural exports, and you've got some good news for consumers.

STEADY PRICES. It's a different story for food processors and farmers. The food companies have tried and failed to push grocery prices upward all year long. For farmers, the hot, dry weather this summer has been severe enough to hurt the harvest, yet not enough to send prices skyward. Indeed, the returns will be spotty because of the vicissitudes of weather. The parched fields of Illinois and Indiana will yield harvests down about 10% from last year, while Iowa, Missouri, and Minnesota actually could see production rise—as much as 12% in Minnesota. The net effect: Even though

many farmers face unproductive fields for the fourth time in 11 years, prices likely will hold steady.

Recent futures prices for September delivery of a bushel of corn have run around \$2.50, right about where they ran at this time last year. The same goes for soybeans. A bushel of September beans recently has traded on the futures market for around \$5.60, not far off the \$6.15 a year ago. Add it up, and because of lower yields, higher costs, and reduced government subsidies, farm income this year will probably drop below \$40 billion, down from

sumers will not accept price increases.

These challenges on the pricing front come at a time when food companies are facing an increasingly finicky consumer. Indeed, food companies more and more are seeing consumers choose private label or discount-priced merchandise. "Many consumers have become quickly trained to look for a deal," notes John Bierbusse, food analyst with A.G. Edwards & Co. in St. Louis. "Purchases are heavily skewed toward people with coupons in the fists." Items most affected by the budget shopping? Cereals, jellies, bread,

and other basic items.

Anticipating the low prices for farm commodities, traders in the futures pits in Chicago sent prices sharply downward when the rain first fell in early August. Then, the Agriculture Dept.'s forecast of low exports—the projected 1.65 billion bushels of corn was down 100 million bushels from July's outlook—was a second boost to the bears.

Don't count the weather completely

out yet. Heavy spring rains delayed planting in the key corn states of Iowa and Minnesota. Late planting means late harvest, and late harvest means vulnerability to an early frost. More than half of Minnesota's corn crop won't mature until after the normal first frost date; in Iowa, the figure is 12%. "That's just the average," says William Biedermann, an analyst with Allendale Inc., a research firm in Crystal Lake, Ill. "If we get an early frost it could be trouble." But for consumers, the midsummer outlook couldn't get much better.

By David Greising in Chicago



AN IOWA SOYBEAN FARMER: WHEN THE RAIN CAME DOWN, SO DID FUTURES

\$47 billion in 1990, estimates Neil Harl, an Iowa State University agricultural economist. "We don't want a handout, we don't want charity," McQueen says. "We just want a fair price for our crops, and we're not getting it."

This time, food companies could end up with the same complaint as farmers. Even though commodity prices are only about 8% of the cost of any packaged product, food companies will normally match any commodity increase penny for penny. "The food companies are normally not bashful about transferring price increases to the consumer," observes Harl. "This year, con-

WHAT'S NEXT— SOVIET BAKE SALE?

Moscow is scrambling to make loan payments it can't afford to skip

It's the \$64 billion question. As Moscow runs critically low on hard currency (charts), will the Soviet Union be forced to undergo a humiliating Third World-style foreign debt rescheduling?

While the Soviets aren't demanding relief yet, Western bankers say Moscow will have to scramble to repay the \$12 billion in foreign loans coming due this year—plus an additional \$5 billion in long overdue bills from Western suppliers. Indeed, says Banque Nationale de Paris Senior Vice-

President Pierre Tailbot, "The Soviets will have to empty every drawer they can find" to raise cash.

Already, Moscow has stepped down on imports. It is selling rubles to Western tourists at the black market rate of 30 to 1 dollar. That's less than half the price only a few winters ago. Yet another move: huge sales of platinum and other metals on world markets. Tony Wark-Ching, a senior consultant at London's Commodities Research Unit Ltd., figures the Soviets have raised \$1 billion this year from metal sales. "It certainly has the look of a fund-raising exercise," he says.

ICK FIXES. These and other maneuvers might avert off a debt shock for the remainder of this year, bankers say. But banks are refusing to lend Moscow any new cash, and Western governments are using to advance the Soviets much more than market change until radical economic and political reforms are put into place. As a result, Moscow is beginning to suggest that it can't keep its debt payments coming indefinitely. One senior Bush administration official says the Soviets recently broached the subject of debt restructuring to Western governments at the July Group of Seven summit in London, only to be told such a move would be unwise, because it would pulverize Moscow's already dismal credit rating. Moscow hasn't given up. On Aug. 6,

Oleg Mozhaikov, foreign currency chief at the Soviet central bank, told reporters that "the need to reschedule exists." What the Soviets envision is a set of Western government guarantees that would allow them to continue paying their debts on their present schedule.

That scenario is less worrisome to European markets than the possibility of a request from Moscow for some form of debt forgiveness, like Poland's or Egypt's. That kind of speculation un-

off Moscow's access to fresh money" just when it needs it the most. At a minimum, the G-7 probably would put on hold the Soviets' bid to join the International Monetary Fund. "Such moves would make Gorbachev's position very difficult indeed," says a Soviet banker.

Perhaps in recognition of that, bankers believe the Soviets are eyeing a slew of methods to preserve their rapidly falling credit standing. The Soviet foreign trade-finance bank has already retired almost half of Moscow's short-term debt by selling gold, digging deeply into foreign reserves, and taking down some \$2 billion in fresh credits. The central bank's Mozhaikov says the Soviet Union is even considering revealing top-secret data on its gold reserves in hopes of securing Western loans with the precious metal. And Moscow is thought to be discussing the sale—at a discount—of

some of its \$60 billion portfolio of loans to such countries as India and Algeria. "There's a market for it," says BNP's Tailbot.

ALARMING. Such moves are only short-term fixes for a struggling economy. Amid sagging oil sales, Soviet exports are running 37% below 1990's level, though Gorbachev has offset that decline somewhat by clamping down on imports. The autumn harvest is expected to be 20% below normal, signaling the need for increased grain purchases abroad. And to make matters worse, an alarming \$30 billion in Soviet external debt is scheduled to come due between 1992 and 1994.

Whether to stave off default or political chaos on their doorstep, such hardships probably will eventually compel the Soviet Union's European neighbors to continue shoveling money Gorbachev's way. Deutsche Bank, for example, is cooking up a \$595 million loan, 98% guaranteed by the European Community, to finance Soviet food imports from Europe. "The Europeans are inclined to prevent the breakdown of the Soviet economy," says Karl Kühne, executive director of Credit Suisse First Boston Ltd. Even without the economic reforms the G-7 is seeking, the West may have to grit its teeth and keep Moscow afloat a little while longer.

By Richard A. Melcher in London and Igor Reichlin in Bonn, with Stewart Toy in Paris and bureau reports



SOVIET OIL EXPORTS ARE WAY OFF



nerves traders in Europe, where French and German lenders alone account for a third of the \$50 billion in bank debt making up the bulk of Moscow's IOUs. In an instant, the value of Soviet loans, now worth 60¢ on the dollar on the London money market, could plummet as low as 15¢—"around where Bulgaria's is"—estimates Peter Hock, a trader at Lazard Brothers Ltd.

Even worse, warns an official at Germany's Bundesbank, any subsequent debt moratorium could "completely cut



THE HONEYMOONERS: SMITH (LEFT) AND ROSENBERG WILL CUT \$1 BILLION A YEAR IN COSTS

BANK OF AMERICA'S BIG BANG

Merging with Security Pacific could make its national dream come true

Grand ambition has defined the culture at Bank of America ever since A. P. Giannini attached that daring name to the small San Francisco bank that he founded back in 1904. But Giannini's dreams were repeatedly thwarted, first by restrictive state and federal legislation during the Great Depression and later by an avalanche of bad loans that forced BofA into a dramatic retreat. Yet through it all, the dream never died.

Now, it's close to reality. On Aug. 12, BankAmerica Corp., its health restored and its ambitions fired by the mergers sweeping U.S. banking, gobbled up Los Angeles-based Security Pacific Corp. in a stock swap worth more than \$4 billion. The combination of BofA and its biggest local competitor will create a megabank spanning 10 states, whose \$190 billion in assets will be exceeded in the U.S. only by Citicorp (table). Says BofA Chairman Richard M. Rosenberg: "This is an historic opportunity to become the leader in American banking."

A model might be more like

it. Rosenberg's king-size deal comes close on the heels of two other record-breaking bank mergers—the \$135 billion marriage of Chemical Banking and Manufacturers Hanover and the combination of NCNB and C&S/Sovran into the \$6.8 billion NationsBank. San Francisco's Wells Fargo & Co. and Los Angeles-based First Interstate Bancorp now may be pressed to follow the BofA-SecPac example, either by hooking up themselves or finding an out-of-state partner. But neither seems to have the national ambitions of BofA. With federal and state restrictions on interstate banking crumbling fast (box), Donald G. Coonley, chief national bank examiner of the Of-

fice of the Comptroller of the Currency predicts that by the mid-1990s, "two or three very large institutions" will top over the pack of regional and local banks. As banks consolidate, he adds, "they will look at the whole country. Clearly, Rosenberg, 61, has that in mind."

There's little doubt that he has a distinct edge on other banks with big plans (table). The new BofA has \$12 billion in capital, a solid base in the fast-growing West, and 2,400 retail branches—already the biggest such network in the nation. Rosenberg probably has the critical mass to move east, an ambition that is no secret. Earlier this year, he bid for the failed Bank of New England Corp. **'ON THE PROWL'** Regulators sold BNE to Fleet/Norstar Financial Group Inc. instead, prompting many analysts to fear that the government wants more regional and local consolidation—at least until Congress gives the go-ahead, perhaps as early as the fall, to full interstate branch banking. Still, BofA executives say they plan to expand eventually into three-quarters of the nation's banking markets. "They are going to be hunters on the prowl," says Donald McNeese, who has advised both Rosenberg and SecPac Chairman Robert Smith at New York-based management consultant Cresap.

This won't be the first time BofA has tried to throw its weight around. Back in the 1970s, it was the largest U.S. bank with an apparent goal of becoming the Bank of Planet Earth. Like cross-country rival Citibank, BofA pumped billions into foreign corporations and shamed Third World governments. But as the 1970s petrodollar boom faded, BofA started to implode. By 1986, the badly bruised giant even had to fend off a takeover attempt by First Interstate.

The comedown prompted a painful restructuring. To help bring it off, BofA's board turned to Rosenberg, then chairman of the bank's Seafirst Corp. subsidiary. Although Citi Chairman John Reed is still trying to pursue global business, Rosenberg has refocused the bank on consumer deposits and retail lending to score an amazing comeback. And he has allowed BofA to think big again.

While Rosenberg's bid to return to his native New England didn't pan out, he has picked up more than a dozen properties, mostly failed thrifts, from Resolution Trust Corp. Earlier this year, after merger talks between SecPac and Wells foundered, Rosenberg jumped in. Says a banker who has known the chairman for years: "Rosenberg is feeling his oats."

ASSESSING THE POWERHOUSE BANKS

Figures are pro forma for all but Citicorp, pending completion of recently announced mergers

Rank	Assets Billions	Equity capital Billions	Reserves*	Branches/ATMs
CITICORP	\$216.9	\$10.2	48%	1,700/2,449
BANKAMERICA	190.0	12.0	70	2,400/4,000
CHEMICAL	135.5	7.7	71	660/977
NATIONSBANK	118.2	6.8	89	1,896/1,641

*As a proportion of nonperforming loans

SOURCE: COMPANY REPORTS, SUTRO & CO.

n merging with SecPac, Rosenberg ns to pump up the combined banks' tom line through a \$1 billion-a-year t-cutting campaign echoing BofA's 'lier retrenchment. Hundreds of nches are expected to be shuttered, l industry experts look for 14,000 or re jobs to be eliminated within three urs, representing nearly 2% of all fi- cial-services jobs in California. The t-cutting could help boost BofA's nings to \$6.25 a share in 1993 and 35 in 1994 from last year's \$4.95, esties Sandra Flannigan, an analyst at x. Brown & Sons Inc.

SecPac's Smith will help Rosenberg lement the cost cuts as his new .2. But it's an open question whether senberg intends to groom Smith as heir. Smith says he would be "happy be the one that's selected when the e comes." But the BofA leader is al- dy high on his own vice-chairmen, o Frank N. Newman and Lewis W. leman, who runs the bank's interna- al business—which many think Ro- berg wants to expand. One banking ert believes any nasty surprises in :Pac's loan portfolio could sandbag ith's chances.

COOLED OFF. Rosenberg declined to be interviewed. But some analysts think :Pac will bring less to BofA than Ro- berg anticipates. Consultant Norman tz of MCS Associates in Irvine, Calif., nks Rosenberg will be hard-pressed to ch his goal of \$1 billion in annual rings within three years.

to do so, says Katz, he'll have to cut erating expenditures to 3.4% of the nk's assets. That's far below BofA's rent 3.86% and SecPac's 3.93%. At %, Wells Fargo is considered the lean- and meanest big bank around.

Even if Rosenberg reaches his cost- ting target, he still will have to con- id with SecPac's loans. Not long ago, was considered one of the nation's test banks, but SecPac cooled off as recession hit the West. With nonper- ming loans and foreclosures rising it, Rosenberg and Smith will set aside extra \$1 billion to cover bad debts. t while traders have bid BofA's stock 16% since the merger was announced, t everyone on Wall Street is totally illed. The credit-rating agency Duff & elps Inc., for one, worries that Sec- c's bad loans could "burden the con- idated entity."

Don't try telling that to Rosenberg. e founder Giannini, he wants to see fA's red-and-blue logo wherever he es. Chances are that he'll see his wish- fulfilled, perhaps even more quickly in he ever thought possible.

By Russell Mitchell and Joan O'C. milton in San Francisco and Kathleen rwin in Los Angeles, with William sgall in New York

Commentary/by Catherine Yang

GREASING THE RAILS FOR THE BANK-MERGER EXPRESS

First came the stealthy forays into the securities business. Now, it's the one-a-week megamergers. Surely and not so slowly, the banking industry is remaking itself. And it's doing so without the imprimatur of legislation from Congress.

That raises the question of what Washington's role should be as the battered industry searches for ways to restore its health. The short answer is:

a supporting role. Regulators should continue to forbear, and Congress should clean up the legislative mess it has made over the years. The industry, perhaps tardily, is attempting to face reality. Lawmakers need to erase Depression-era laws that prevent banks from making business decisions that could solve their woes.

MAKE A WISH. The moves banks have made so far are steps in the right direction.

By closing bank branches and combining back-office operations, merged banks can cut costs and help stem incessant losses. "There's no question that these large-bank combinations are good for the banking system," says James J. McDermott Jr., president of Keefe, Bruyette & Woods Inc. "They are creating stronger, better-earning institutions." That means we'll see more linkups such as the mergers of Bank of America and Security Pacific, Chemical Bank and Manufacturers Hanover, and NCNB and C&S/Sovran.

Those gargantuan deals should go through with surprisingly little comment from Washington. Aside from assuring themselves that the big new banks have adequate capital, the regulators mostly have been cheerleaders, strongly endorsing bank consolidation. Federal Reserve Bank of New York President E. Gerald Corrigan, for instance, sent a clear message at a New York State Bankers Assn. meeting in January, when he praised the cost savings and business synergies in mergers. "I would be very surprised—perhaps disappointed—if when we meet here next year, one or more mergers among the largest banks in the U.S.

are not already a reality," he said.

He got his wish in spades, without overt government intervention. "It's essentially a private-sector decision," says Federal Deposit Insurance Corp. Chairman L. William Seidman. "We're not the matchmakers."

And they're not home wreckers. Not long ago, the sheer size of the deals—the new Bank of America will be the second-largest bank in the country,

with \$190 billion in assets—would have set off alarms at the Justice Dept.'s Antitrust Div. Tot up the mergers already announced, plus the others now in the rumor stage, and the nation's seven biggest banks could soon control about a third of U.S. banking assets.

NEW LOANS? The trust-busters don't blink at that number because they no longer see banks as the only players in the savings-and-lending business. Now,

nonbank companies, including local credit unions, GE Capital, and American Express, count, too. Such competition ensures that consumers aren't likely to be hurt by the new banking giants. In fact, consumers and businesses alike could eventually benefit when chastened banks start making loans again rather than pumping money into their shriveled capital bases.

If this be the fruit of the regulators' benign neglect, what should Congress do? Should it, too, just butt out? Not at all. Congress is one place in official Washington where action on banking is long overdue. Lawmakers, who have been wrangling over bank reform for years, should finally dismantle the nation's outdated banking laws. Congress should let banks move freely across state lines and offer other financial services such as securities underwriting and insurance. That way, banks can adopt strategies based on the needs of the markets, rather than on rules drafted in Washington.

The industry may need a radical restructuring to solve its financial ills. Congress should smooth the way, and the rest of Washington should do what it does best: nothing.



THE FED'S CORRIGAN: BACKING BANK CONSOLIDATION

'WHEN I'M DOWN AND OUT, YOU OWE ME A DRINK'

Icahn forces Delta to sweeten its Pan Am bid by \$361 million in cash

When it was over, all Carl C. Icahn could do was grin his puckish grin. Once again, the chairman of near-bankrupt Trans World Airlines Inc. had swooped down on an otherwise starchy bidding contest. And once again, he'd made life miserable for a conservative set of Main Street executives. Icahn lost the battle for Pan

American World Airways Inc., but not before forcing Delta Air Lines Inc. to wade in deeper than it planned. "When I'm down and out," Icahn told Pan Am's happy creditors as he threw in the towel, "you owe me a drink." Icahn's aggressive presence in the two-month contest for Pan Am forced Delta Chairman Ronald W. Allen to pay \$361 million more in up-front cash than he had first bid. And despite fierce opposition to taking on any Pan Am liabilities, Delta wound up assuming \$749 million in obligations and agreeing to finance a smaller, ongoing Pan Am focused on Latin America. Delta does get Pan Am's European routes, its shuttle, and its Frankfurt hub—assets key to keeping pace with rivals American Airlines Inc. and United Air Lines Inc. internationally. But in uncertainty alone, the cost was high.

MAGIC ACT. Delta's rich price was a direct result of Icahn's uncanny knack for pulling credibility out of a hat. Despite his status as chief of an embattled airline in the throes of arranging its own recapitalization, Icahn crafted a last-minute, \$1.4 billion bid with impeccable credentials: \$400 million in cash from United and American, the nation's two largest airlines. Icahn knew that neither wanted to pick up Pan Am's liabilities or keep its employees—requirements demanded by Pan Am's creditors. So he agreed to take on the bulk of the liabilities himself, luring United and American with a vow to sell them various European assets after the deal was done.

To fend off its three rivals, Delta upped its bid. A lot. It agreed to a package valued by Pan Am and its creditors

at \$1.37 billion in cash and assumed liabilities. The creditors figure the deal should return them 10¢ per dollar of claim, maybe 15¢. Not much, but it beats a prognosis of zero return when Pan Am first filed bankruptcy.

While Delta agrees the creditors will get \$1.37 billion, it insists that its bid will amount to less than \$600 million in actu-



PAN AM'S PLASKETT AND DELTA'S ALLEN: A \$1.37 BILLION DEAL

al cost over the long term. Here's how it works: Delta's total cash outlay will be \$621 million. Of that, \$416 million will pay for European routes, the shuttle, 40 jets, and a slew of spare parts. Delta will also pay \$50 million for a 45% stake in the new Pan Am, while accepting a \$155 million note from the new company.

Meanwhile, Delta will extend \$100 million in credit to the new Pan Am and

Delta's rich price was a direct result of Icahn's uncanny ability to pull credibility out of a hat

give the reorganizing company an \$80 million loan. It will assume \$360 million in liabilities associated with Pan Am participation in the U. S. Air Force's Civil Reserve Air Fleet (CRAF), \$100 million in outstanding ticket liabilities, and \$100 million in miscellaneous liabilities. Finally, Delta said it would cover any Pan Am loss over \$140 million between August 12 and Dec. 1, to a limit of \$100 million.

To cut the \$1.4 billion total below \$600 million, Delta told analysts it could resell \$50 million of the spare parts and take care of about half of the \$100 million ticket liabilities on its own flights. As for the \$80 million loan, that must be paid back under bankruptcy law. All that sounds reasonable. But take a look at the other items in Delta's calculations.

TICKET SALE. As for the loan guarantee, Delta is betting that more certainty about Pan Am's future will increase traffic and help stem a flood of red ink that neared \$100 million in June and July alone. To entice passengers, Pan Am Chairman Thomas G. Plaskett has launched a 25% sale on all tickets. Delta has told analysts it won't have to make good on its guarantee. That seems optimistic given that June and July are two of the carrier's strongest months, and Delta is on the hook for almost four months in a slower season.

Delta also assumes that the new Pan Am—a smaller carrier pitted directly against American in Latin America—will pay back the \$155 million note and whatever it uses of the \$100 million line of credit. But since Delta at first had no interest in the Latin American division, its potential is unclear.

And for Delta to avoid paying the \$360 million CRAF liability, the new company will have to fly the 12 Pan Am 747s devoted to the CRAF program. Old air ill-suited to the Latin American route they won't do much for the new Pan Am's profits.

Delta also must worry about training 6,600 new workers and the costs of developing the new routes. That is, those can keep: Northwest Airlines Inc. may persuade regulators to force Delta to give up a Detroit-London route it covets.

In any case, the deal surely jumps starts Delta's slow push into Europe while adding \$1 billion in fresh revenue immediately. Thanks to Carl Icahn, Delta has paid dearly for the chance.

By Michael Oneal in New York, with Lisa Driscoll in Connecticut

ANNA SUE RJR NABISCO? ET IN LINE

ss actions charging fraud during the buyout could win big awards

has been nearly three years since the King Kong of leveraged buyouts, out lawsuits spawned by the take- of RJR Nabisco Inc. keep piling up. The latest, filed in Charlotte in early 1988, the president of the 16-campus university of North Carolina system ns he personally lost \$19.7 million use he sold RJR stock even as for- RJR Chairman F. Ross Johnson was dulently hiding his LBO plans.

ne court filing by Clemmie Dixon ngler Jr. so far has drawn scant no- from RJR watchers on Wall Street. as a \$2 billion class action nearing lution in New York that makes simi- claims. Analysts have spent more e worrying about product liability ns related to the cigarette sales of s R. J. Reynolds Tobacco Co. unit.

NUMBERS. Such inattention might re- in a nasty surprise. If the class ac- clears an important procedural hur- in the next few weeks, RJR one day be forced to pay an unexpectedly e settlement to avoid a jury trial. eover, Arthur N. Abbey, the lead rney in a separate class action in aware over how the final auction for was conducted, says he's within s of a settlement that will reach is of millions of dollars."



which won RJR in the \$25 billion bidding war, want to get the litigation behind them. "Plaintiffs' lawyers love to throw around big numbers that bear no relation to the merits of their cases," says Lawrence R. Ricciardi, executive vice-president and general counsel of RJR. "I haven't lost any sleep."

So far, Ricciardi has had little cause for insomnia. In the most widely followed case, RJR finessed a challenge by Metropolitan Life Insurance Co. With a 1988 lawsuit, the insurer vowed to strike a blow for bondholders whose securities often were devalued by LBOs. But instead of a big cash settlement, MetLife quietly agreed to a deal in January that permitted it to swap \$30 million in pre-buyout debt for RJR equity.

But the issues raised in the Spangler case could prove more troubling—and offer sweet revenge to the North Carolinian. In the best-selling account of the buyout, *Barbarians*

at the Gate, Johnson's recollections painted Spangler, then a big RJR shareholder, as a buffoon. But in his lawsuit, Spangler makes a case that far from being an off-the-wall proposal, the LBO idea he first brought to Johnson in early 1988 by that February had won a tentative funding commitment from Citibank. Spangler, who made a fortune in the construction business, bought 1.1 million shares of RJR stock in 1985 after selling a chain of motels. His family also is the largest single shareholder at NCNB Corp., with a stake in the bank valued at more than \$300 million.

After Johnson spurned his proposal, Spangler dumped nearly a third of his RJR holdings at an average price of \$54 a

share in September and October, 1988, for a total of \$19.5 million. But Johnson and his top advisers decided to pursue an LBO in mid-May, 1988, or earlier, Spangler alleges. Johnson's initial \$75-a-share buyout plan was announced on Oct. 20 of that year, and six weeks later, KKR won the bidding at \$109 a share.

Spangler maintains he wouldn't have sold the shares if Johnson had properly disclosed his pending buyout plan. He wants RJR and Johnson to make up to him the \$19.7 million difference. Johnson, who now operates a boutique consulting and investment company in Atlanta, RJM Group Inc., left word with his secretary that he has no comment on the litigation.

**JOHNSON:
QUOTED IN A
BOOK ABOUT
THE BUYOUT,
HE PAINTED
SPANGLER,
THEN A
BIG RJR
SHAREHOLDER,
AS A BUFFOON.**



The larger class action offers even more allegations about Johnson's LBO plans. It claims that long before KKR's Henry Kravis broached the idea at a September, 1987, dinner, Frank A. Benevento II, a onetime Lehman Brothers investment banker who was retained by Johnson for strategic planning, had been working on various LBO scenarios. And the lawsuit claims that Spangler's approach was spurned because Johnson did not want it to interfere with his own plans to lead an LBO with Shearson Lehman Brothers Inc.

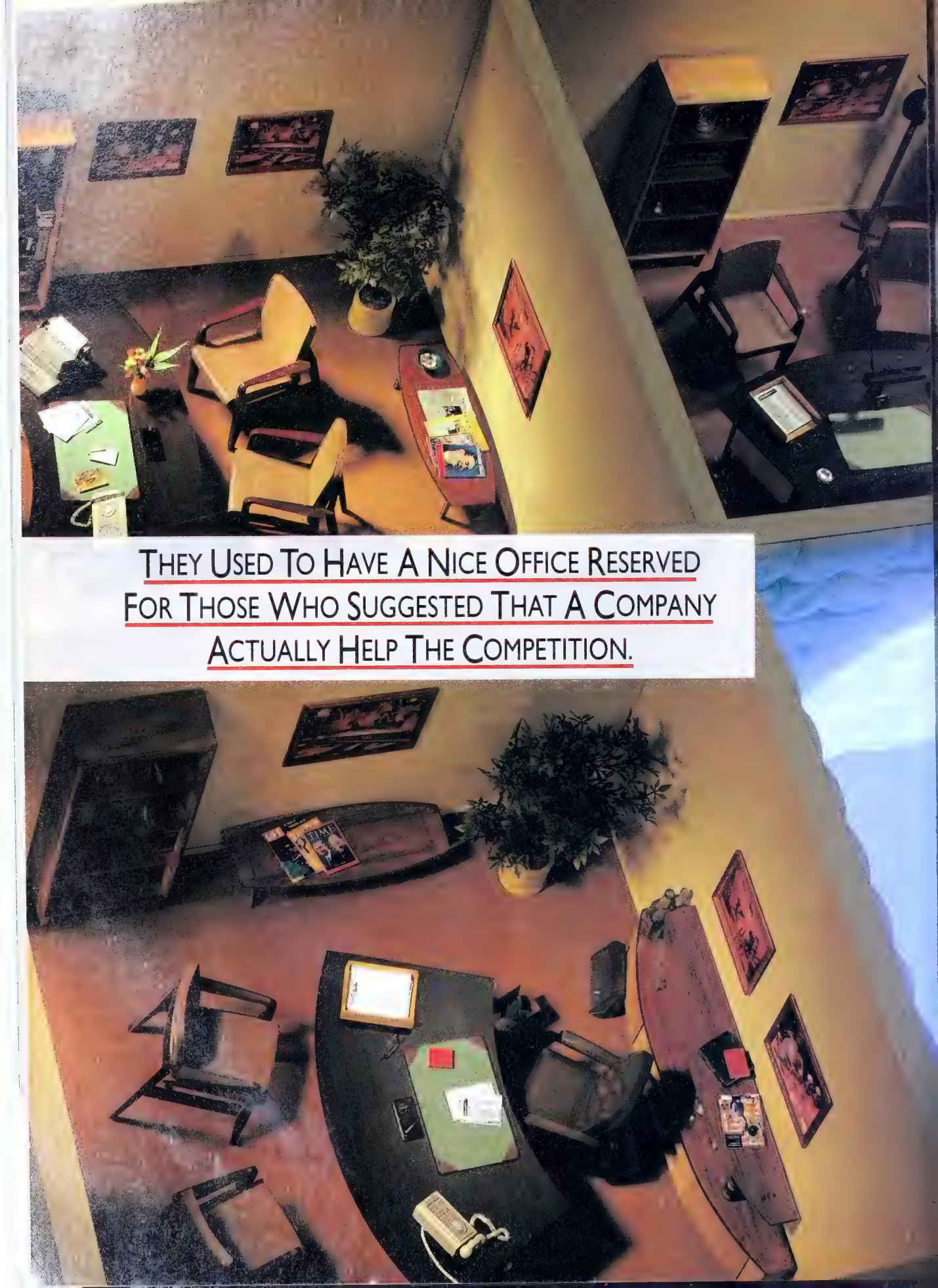
'VERY NERVOUS.' A judge in New York granted class action status to the larger case in March. He's expected to rule soon on a motion by RJR that the entire case be thrown out. If the judge allows it to proceed, securities law experts predict settlement talks would soon get serious. "Defendants get very nervous having jurors, who are naturally suspicious of corporations, deciding the matter," says Columbia University law school professor John C. Coffee.

Spangler, who's not talking about RJR, could have stayed quietly in the background and taken a chance on the larger class action. But by filing his own suit, the man Ross Johnson made out to be a buffoon hopes to get the last laugh.

By Chuck Hawkins in Atlanta

**SPANGLER:
HE CONTENTS
THAT JOHNSON,
THEN RJR
CHAIRMAN, HID
HIS PLANS FOR
THE COMPANY
AND COST
SPANGLER
MILLIONS**

RJR disputes the charges in all of these s. And given the size of RJR, it's hard envision any bad news from its law- s crippling the company. Sales this r should top \$15 billion, and a recent r-for-equity swap will reduce its an- l interest tab by about \$1 billion. Yet agers installed by the buyout firm Kohlberg Kravis Roberts & Co.,



THEY USED TO HAVE A NICE OFFICE RESERVED
FOR THOSE WHO SUGGESTED THAT A COMPANY
ACTUALLY HELP THE COMPETITION.



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Crazy to believe that our industry
will be healthier - and our customers
much better off - if we all work
to cooperate rather than compete.

Crazy to establish the first
Technical Support Alliance,
a group of hardware and software
manufacturers (among them,
some of our archest rivals) with just
one mission: to help people
solve their service problems.
Whether the problem is with
IBM, Microsoft, Novell, or
any other member of the alliance.

Sure. Call us crazy. But before
you do, remember this:
more different kinds of computers
talk to each other through
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EQUIFAX' EXIT MAY NOT TAME THE CONSUMER BACKLASH

Congress could put broad limits on the sale of credit data

Some people are surprised to find out how much information about their lives is stored in corporate data banks. The level of detail goes well beyond their annual income and credit rating all the way down to their height, weight, and marital status. It's all in a computer somewhere and available, for a small fee, to total strangers. That's news to many consumers, but they're learning—and the backlash is growing.

Equifax Inc., a leading compiler of credit information, is feeling the sting. On Aug. 8, the Atlanta-based company, bowing to pressure from consumer groups, declared that it would no longer sell detailed, personal information about consumers to direct marketers, the folks who flood your mailbox with envelopes marked "urgent" or "value packet." "People see the use of this information as a privacy problem if it goes beyond credit purposes," says John A. Baker, Equifax senior vice-president.

Equifax really doesn't have much to lose by exiting the direct-marketing business. Its Consumer Marketing Database products brought in only about 1%, or \$12 million, of the company's more than \$1 billion in revenues last year, says Baker. The company, he adds, will keep its \$250 million business of selling lists of creditworthy consumers to financial institutions trying to sell such things as MasterCard and Visa accounts.

RISKY BUSINESS. There's an important difference—other than revenues—between the business Equifax is keeping and the one it's dropping. The selling of data on consumers' creditworthiness to banks is part of Equifax' core business of credit approval. Few consumer advocates or legislators would block banks from using credit data to determine who should receive unsolicited credit-card applications. The trouble comes when Equifax and other credit-information collectors sell the same lists of creditworthy consumers, along with details about their shopping and lifestyle habits, to companies that hawk clothing, insurance, and other products.

It's worse than sneaky for credit bureaus to collect credit data for such purposes, according to the Federal Trade Commission. It says such practices should be illegal. And Congress may explicitly make them so. As early as Sep-

tember, consumer affairs subcommittee Chairman Esteban E. Torres (D-Calif.) plans to introduce legislation to strengthen and update the 20-year-old Fair Credit Reporting Act. Congress' target isn't all direct marketers: Hundreds of companies would be allowed to continue trading in consumer data.

But mixing credit data with lifestyle data could become a no-no. "We're concerned that this mixture smacks of a direct invasion of privacy," says Albert Jacquez, subcommittee staff director. The legislation may also ban the use of credit reports by employers when making hiring decisions, Jacquez says.

Besides trying to stave off sweeping new regulations, Equifax is also trying to distance itself from TRW Inc. and Trans Union Corp., its much bigger com-



TORRES: LEADING A CONGRESSIONAL CRACKDOWN ON CREDIT REPORTING

petitors in consumer data-base marketing. Both of those companies say they'll continue to mix credit data with personal information. That's a precarious business to be in, especially since states have filed suits against TRW in July, charging the Cleveland company with privacy violations as well as inadequate consumer service. TRW says the charges are groundless and is contesting them.

The Equifax exit won't visibly reduce the number of catalogs, special offers, or telemarketing calls received by the average consumer. But other companies might follow suit, and that could actually be good for business. A study published last year by Equifax found that 71% of Americans believe that they have lost all control over how information about them is collected and used by companies. If consumers start feeling that they're regaining control, they might look more closely at all those sales pitches in the mail.

By Evan I. Schwartz in New York, with Walecia Konrad in Atlanta

ENTREPRENEURS

THE DIRT DEVIL MADE ROYAL DO IT

The way consumers go for its vacuum cleaners, it just had to take off

In the 1980s, LBOs certainly got a bad rap. But tiny Royal Appliance was one that has worked like a charm.

John A. Balch and a group of investors got the vacuum cleaner company for a mere \$4.5 million in a 1981 leveraged buyout. Not bad, especially since it came with more than \$1 million in cash in its treasury. Better yet, in early August Royal Appliance Manufacturing Co. went public with a \$100.7 million offering of stock. It hit the market at an initial price of \$15.50 and immediately shot up \$4. Investors had been tempted by the devil—the Dirt Devil. For the past seven years, the Dirt Devil Hand-Vac has kept

Royal in the appliance industry spotlight.

Royal was no newcomer to vacuum cleaners. It sold its first models in the early 1900s. But after a string of uninspired owners and even a dip into bankruptcy in 1953, Royal's expensive and unwieldy metal models were losing lighter plastic rivals. In 1979, Royal's 8-year-old president, Stanley E. Erbo, died at the company water fountain.

Balch then was a vice-president for finance at Cleveland medical devices maker Technicare Corp.

He had seen Johnson & Johnson buy his employer, and that kindled in him a desire to run his own show. By December, 1981, after his investment group bought



yal from Erbor's estate, he was doing t that.

He hired a marketing staff and got yal's sluggish sales force back in the d. He took the company's handheld tal vacuum and made a cheaper mod-in plastic, thus creating the original t Devil, whose old-fashioned styling kes it look like a relic from your ther's broom closet. Short of capital, eh hired outside component suppliers. e're an assembly operation," he ex-ins. "We don't make anything." A 7-American devotee, Balch purchases less than 95% of his parts in the S.—unlike many rivals. To keep cus-ers happy, Royal imprints a toll-free nber on each vacuum, inviting con-ners to call with problems and ques-ns. Balch handles some calls himself. He became a marketing whiz and nt heavily on national advertising—.5 million in the first half of 1991. He is Dirt Devil TV and print ads nation-7, as well as radio spots on the syndi-ed Paul Harvey show. Balch also cul-ated lucrative contracts with mass ailers such as Wal-Mart Stores Inc., shing Royal's sales above \$120 million 1990, up from \$6 million in 1982. With its revolving brush, the Hand-e cleaned up on rivals. The bright red um has hotly challenged Black & cker Corp.'s DustBuster, the cordless nnder and innovator of the portable cept. Black & Decker was forced to roduce its own plug-in, revolving-ish model this year.

Y PROFIT. Royal markets a full line of t Devil products, spanning the up-ht, canister, and push-sweeper cate-gs. As Royal matures, similar success y prove harder to come by. "They ked up Wal-Mart, K mart, then Tar-, so they grew, grew, grew," says e competitor. "But that's done now." nifer Baker Fischback, a marketing e-president, disputes that, pointing to ves of new products she expects will ld plenty of new growth. "We've got t of good years left in us," she says. Royal's initial investors, a group of veland business executives, have won dsome rewards—a full \$54.2 million he IPO, as well as dividends along the y. As for Balch, he has kept a 19% ke, worth about \$37 million.

Balch isn't letting success swell his id. He idolizes Wal-Mart Chairman n M. Walton and his legendary lack pretentiousness. So he has practically ndated modesty at Royal. "It's kind our image," explains Fischback. "We not to hire snots." Or, as Balch puts n one of his favorite slogans, "When i're in the business of picking up dirt, a gotta stay pretty low to the und." With the IPO, however, that obtrusive cover is blown.

By Maria Mallory in Pittsburgh

THE LAW

SO MANY LAWYERS, SO LITTLE OPPORTUNITY

Even prestigious firms are hurting—a tough break for the class of '91

Could this be a dream? Mary Diepenbrock was all set to go to work for the law firm of Thelen, Marrin, Johnson & Bridges after graduation from McGeorge School of Law in Sacramento. Then last spring, the San Francisco office offered her and 14 other new law grads the chance to delay their starting dates in return for cold cash. Diepenbrock grabbed the \$10,000 and is extending her post-bar-exam travels by three months.

No, it's not a dream. Instead, Diepenbrock demonstrates the current nightmare in the law biz. Battered by recession and cost-conscious clients, firms that fattened up in the 1980s are hurting. They're deferring starting dates for new hires, rescinding job offers, and cutting short cushy summer-intern programs. Even 1991 law grads who can boast jobs are sweating. Already, outplacement counselors say, some members of the class of 1990 have gotten the ax. As Diepenbrock says, times are "horribly tough."

NASTY SHOCK. This year's recruiting season, which is getting started already, promises to be even worse than last. Firms are traveling to fewer schools and sending fewer recruiters. Even the most prosperous firms don't expect to hire as many lawyers. Normally, firms must guess their hiring needs a year in advance—third-year law students who snag jobs this fall won't begin until September, 1992. This season, firms are being overly cautious because of uncertainty about the economy. At the University of Michigan Law School in Ann Arbor, Placement Director Nancy Krieger expects a drop of up to 20% in the number of firms visiting the school. That figure, she says, is typical of the experience at other law schools around the U.S.

Since it's no longer a seller's market, law students from New York University to the University of California at Los Angeles are scrambling. In May, incoming associates at Manhattan's Webster & Sheffield were shocked when the firm

reneged on its offers of full-time jobs. Weeks later, the firm collapsed. Five second-year students at the University of Texas School of Law in Austin last spring had firms yank their summer jobs at the last minute. In good times, these spots almost inevitably led to full-time positions after graduation.

Rescinded offers and job deferrals were "virtually unheard of until this year," says Lujana Wolfe Treadwell, executive director of the National Association for Law Placement. But so were

the massive layoffs of associates and partners that have rocked even the most prestigious law firms.

At Skadden, Arps, Slate, Meagher & Flom, executive partner Peter P. Mullen denies widespread rumors of massive layoffs this year. But Mullen admits that the firm has slowed its recruiting of new lawyers, toughened associate evaluations, and held the line on raises. Mullen says "there's a chance" that Skadden

or some other top New York megafirm may cut the going rate for starting salaries. It's now up to \$85,000.

All this doom and gloom hasn't scared away law-school applicants. Since the mid-1980s, law schools have pumped out some 35,000 new graduates annually. And an unprecedented 94,000 applicants are competing to enter law school this fall, the fourth consecutive year to set a record, according to Law School Admission Services.

One reason is obvious: moolah. Despite the sharp downturn in legal business last year, associates in U.S. firms with 75 lawyers or more earned an average of \$69,000, says a new survey by consultants Altman Weil Pensa Inc. For many college grads, law school also puts off pounding the pavement during a recession. And while the legal market is contracting now, it may be booming by the time today's law students are up for partnership. Alas, they may never have the chance to get paid for not working.

By Michele Galen in New York, with Wendy Zellner in Dallas



By D. Br H. and J. L. W. 2008

CLIFFORD AND ALTMAN GET OUT OF THE KITCHEN

► The Aug. 13 resignation of the two top executives of First American Bankshares could clear the way for a quick sale of the company. Chairman Clark Clifford and President Robert Altman found their jobs in jeopardy as soon as the Federal Reserve charged in March that First American was secretly owned by Bank of Credit & Commerce International, the rogue international bank. Both men deny knowledge of the BCCI link.

Nicholas Katzenbach, a former U.S. Attorney General, will succeed Clifford. A big part of his job is to sell the \$11 billion bank. "We hope to have this thing wrapped up in a very short while," says a top Fed official. The fight over the proceeds will go on much longer, pitting First American's nominal owners against BCCI depositors, other creditors, and the Fed, which has slapped BCCI with a \$200 million fine.

WALLS RATTLE AT ALCOA

► The recent abrupt departure of Alcoa's veteran president was the tremor before the quake. On Aug. 9, Chairman Paul O'Neill imposed a dramatic management reorganization at the world's largest aluminum maker. O'Neill aims to make Alcoa one of the nation's most decentralized large companies. He wiped out two layers of management that separated his office from front-line operations managers. The theory: Quality and customer service will improve dramatically.

START THE PRESSES— THE TRIB LIVES!

► The *Tribune* in Oakland, Calif., has been saved from the grave. On Aug. 14, owner

and publisher Robert Maynard announced a three-way deal for the 117-year-old paper. The key player in the rescue: the Freedom Forum, Allen Neuharth's nonprofit foundation.

Maynard bought *The Trib* in 1983 from Gannett, where Neuharth was chairman until 1989. He financed the purchase with a \$17 million loan from the media giant. He has been in default on the debt, which has grown, with interest, to \$31.5 million. Now, Gannett has agreed to retire the debt in exchange for \$5.5 million in preferred stock in *The Trib* and a \$2.5 million note guaranteed by the Freedom Forum. *The Trib*'s death would have made Oakland the largest U.S. city without a daily paper.

BILL FARLEY GIVES UP A PIECE OF FRUIT

► One of the bigger takeover messes of the 1980s has finally been tidied up. On Aug. 13, Farley Inc. sidestepped a contentious Chapter 7 bankruptcy proceeding, reaching a deal with creditors that exchanges \$172 million of subordinated notes in Farley Inc. for 3 million shares of Fruit of the Loom and a 9.2% stake in Doehler-Jarvis, a midsize metalworking company. Takeover investor William Farley, who long clung to majority control of Fruit, will see his personal

HAIR TODAY, A JOB TOMORROW?

It's a truism in economics that someone profits from even the gloomiest of economic times. During the Great Depression, movie theaters packed 'em in as people sought escape, if only for a few hours, from grim reality.

That was perhaps a more innocent era. These days, as that camera ad says, "image is everything." Which probably helps explain why Dr. Gary Hitzig's business is booming. A New York surgeon who specializes in hair transplants, Hitzig is working his tonsorial magic on laid-off stockbrokers, accountants, and bankers seeking a more youthful look before their next job interview.

These new clients spend \$1,500 to \$7,000 of their severance packages at Hitzig's clinic. Says Hitzig: "I'm learning more about the financial world than I ever knew before." And if you told him this recession was a hairy one, he'd probably just smile and agree.



voting power drop to 33%.

Big winners in the deal include those Farley retirees who belonged to the United Auto Workers. Their medical plan will be secured by 2.4 million Fruit shares.

IT'S LTV CREDITORS VS. THE FEDS

► The Pension Benefit Guaranty Corp. is pulling rank in its effort to get LTV to fund its three pension plans. On Aug. 12, the PBGC ordered LTV to immediately make scheduled contributions to its plans. LTV, which is in Chapter 11 reorganization, suspended the

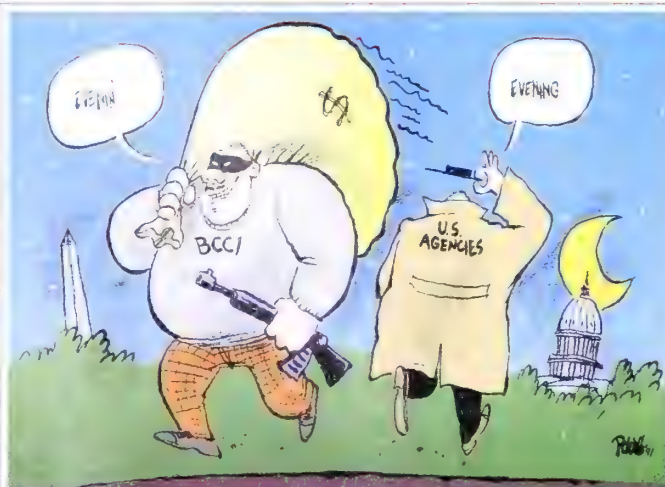
payments after its creditors objected.

Those creditors contend that the PBGC has an unfair advantage over others who claim on LTV's assets. In response to their opposition, LTV has agreed not to continue to fund the plans without the approval. Now, it's up to the federal court in New York to decide whether to require the payments.

PEUGEOT AND STERLING PULL OUT OF THE U. S.

► With U.S. car sales mirroring the worst slump in a decade, France's Peugeot and Britain's Sterling Motor Car, a unit of Rover Group, have decided to bail out.

Peugeot's U.S. sales reached their peak in 1987 when it sold 20,007 cars, mainly diesels, and it never found a niche after diesels went out of favor. Sterling's luxury sedan, which went on sale starting in 1987, suffers from quality problems, such as leather interiors that turn green in bright sunlight. Through July, with over a year of U.S. car sales off 13%, Sterling sold only 1,878 cars, down 28% from a year earlier. Peugeot's sales fell 17%, to 2,200 cars, in the same period.



CONGRESSIONAL REFORM? DON'T START SNICKERING YET

Don't look now, but Congress is gearing up for another of those fitful efforts to reform itself. A bipartisan group of lawmakers—led by Senators David L. Boren (Okla.) and Pete V. Domenici (R-N. M.), and by Representatives Lee H. Hamilton (D-Ind.) and Willis D. Gradison (Ohio)—wants to hack away at the bureaucratic kudzu that angles the Hill. "Congress is in trouble as an institution," says Boren, who wants to streamline the huge number of committees and the bloated congressional staff system that costs taxpayers \$3 billion a year.

The group is pushing for a new 20-member reorganization committee—with its own budget and aides, of course—to sift through reform proposals. The initial response has been predictable: snickers in the cloakrooms. "The committee could just commend its own dissolution," ventures one House subcommittee chairman. "That would be progress."

But while it's easy to dismiss the effort, the Hill leadership is soon set to embrace calls for a sweeping overhaul that would strengthen the leaders' ability to enforce discipline. Power is now diffused among committee chairmen. While the leadership doesn't want to rile the congressional barons now, public support for change, Hill sources say, is working around the scenes to urge on the four reformers. "There's a reasonable chance the leadership will support the group" publicly, later on, says Thomas E. Mann, a congressional expert at Brookings Institution.

Backbenchers also may endorse reforms. They know their institution doesn't work anymore. The number of committees and subcommittees in the House alone has swollen to 195. Jurisdictions overlap, aggravating the already difficult enactment of bills must survive to be enacted. Although the bankruptcy insurance fund is nearly broke, for example, a measure to replenish it is languishing as it goes through five committees.

This kind of stalemate is one reason the public holds Congress in low esteem. Lawmakers believe an overhaul could help refurbish Congress' image. But the rank and file also fear spread of term-limitation measures, which have been ap-

proved in California, Colorado, and Oklahoma. Some 20 other states are mulling similar moves. And there's nothing like the threat of moving men to concentrate a politician's mind.

By Paula Dwyer

THE BABY BELLS ARE MAKING THEIR MAMA NERVOUS

A powerful coalition that has kept the Baby Bells safely inside a legal playpen since the 1984 breakup of the Bell system is about to crumble. When the next battle over communications legislation begins in earnest after Labor Day, the big loser could be one of Washington's premier political players: American Telephone & Telegraph Co.

Judge Harold H. Greene altered the political landscape with his July 25 decision to allow the local phone companies to enter the \$100 million-a-year information-services business. That gives the Baby Bells leverage as Congress mulls a measure that would set the ground rules for their entry into such electronic services as videotext. The legislation is expected to be combined with a Senate-passed bill that would let the companies make telecommunications gear. The Bells had argued they could help maintain America's technological edge.

In the past, AT&T has joined with the newspaper industry to keep the Bells hemmed in. AT&T feared competition in equipment, and newspapers worried that electronic Yellow Pages would compete with advertising. But lobbyists now expect the Bells to cut a deal with the American Newspaper Publishers Assn. that would leave AT&T out in the cold. The Bells would agree to modest curbs on their information services—but only if the newspapers stay on the sidelines during the expected fight with AT&T over entry into the \$75 billion-a-year equipment business. Without newspaper publishers visiting congressmen and printing editorials opposing the legislative drive, it will be tougher for AT&T to stop its offsprings' onslaught.

By Mark Lewyn

PITAL WRAPUP

DLITICS

Arkansas Governor Bill Clinton is looking more and more like a candidate for the Democratic Presidential nomination. BUSINESS WEEK has learned that the five-term governor is wrapped up Robert A. Farmer, treasurer of the Democratic National Committee and chief moneyman for the 1988 Dukakis campaign, as his top fundraiser. Farmer won't comment beyond that coup, Clinton surrogates at the Democratic Leadership Council, a group of moderates, have begun seeking advice from party pros about a campaign manager. Meanwhile, Senator Lloyd Bentsen (D-Tex.), the party's

1988 vice-presidential nominee, has indicated that he would be willing to head the ticket in '92 if Democrats need a unifying candidate.

TAXES

The battle over the tax treatment of intangible assets, such as customer lists, may be resolved soon. The Treasury Dept. and many business groups like a plan by House Ways & Means Committee Chairman Dan Rostenkowski (D-Ill.) to allow intangibles to be written off over 14 years. The General Accounting Office also backs depreciation over a set period. Still unresolved: how to treat the costs of creating goodwill, such as advertising.

CAMPAIGN FINANCE

Fund-raising results from the first half of 1991 show Republicans once again outgunning Democrats. Democratic campaign committees took in a mere \$9.7 million to the GOP's \$40.9 million. Individually, the war chests of Senators Arlen Specter (R-Pa.) and Alfonse D'Amato (R-N.Y.) are bulging with \$2.6 million each. Minority Leader Bob Dole (R-Kan.) has \$2 million, suggesting that he'll run next year despite contrary rumors. Senator Warren Rudman (R-N.H.) has only \$50,000, fueling speculation he won't be back. Likewise for North Carolina Democrat Terry Sanford, who has only \$70,000 on hand.

HIDDEN JAPAN

**THE SCANDALS START TO REVEAL
HOW THE SYSTEM REALLY WORKS**

For months, Japan's top financial reporters had been nosing around giant Nomura Securities Co., hoping to follow a money trail they suspected might lead to the country's power brokers. But only when disgruntled middle-level bureaucrats at the National Tax Agency began to talk did the scandal break wide open. Soon, newspaper headlines were screaming that Nomura and its three big competitors were making paybacks to clients and funneling millions of dollars to one of Japan's most notorious gangsters.

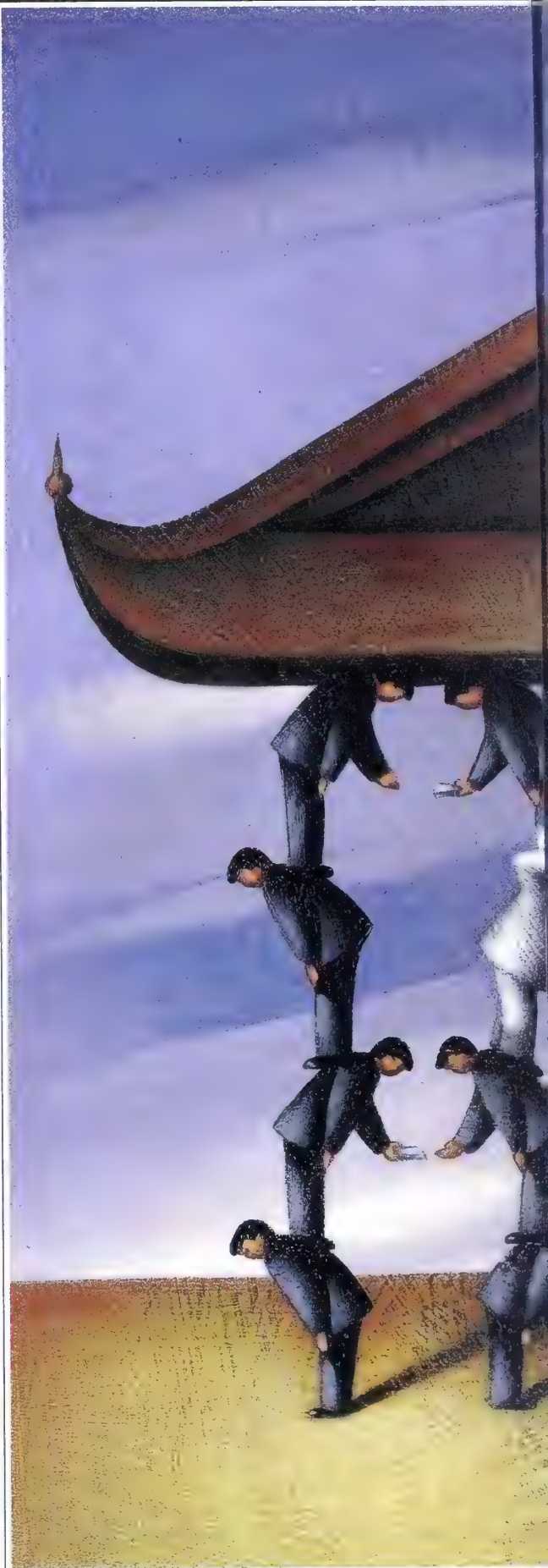
So began one of the worst scandals to rock Japan in recent years. As the revelations are uncovered, a veil is being lifted on the hidden Japan. The scandals are exposing, as never before, how politicians, bureaucrats, big business, and sometimes even gangsters work hand in glove to keep the economic engine primed.

To outsiders, Japan may seem corrupt. But what would amount to scandal in the West is often business-as-usual in Japan. Japan-watchers call it "structural" or "institutional corruption" that helps grease the wheels of the nation's amazing economic machine. "The danger in calling it corruption is projecting onto Japan our own values and legal assumptions," says Chalmers Johnson, a leading Japan scholar at the University of California at San Diego. "What's been revealed is the way business has been done for years in Japan. It's not necessarily bad."

RIPPLE EFFECT. That would be all right if Japan were a third-rate economy. But with Japan's growing piece of the global pie, the scandals are reverberating far beyond Tokyo. Foreigners wanting to do business in Japan are getting a good look at the collusive network they're up against. And those stung by Japanese competition back home are now glimpsing what underlies Japanese corporate prowess. The scandals are again raising the troublesome question: Is Japan's economic system compatible with the rest of the world's?

It's now clear that Japanese and American companies are not on an equal footing. Hitachi Ltd.'s stock market investments, for example, were all but insured by Nomura. As the scandals have now exposed, the broker forked out \$16 million to cover Hitachi's losses over the last couple of years. General Electric Co., by contrast, has no such safety net. No foreign investors were offered paybacks by Japan's Big Four brokers for losses. In fact, several are now mapping lawsuits against the Big Four.

Perhaps most eye-opening is the realization that the Japanese system is based on personal relationships rather than





the dispassionate enforcement of laws. Bureaucrats play a confusing role as both coddlers and regulators of industry. Even everyday life is full of rituals that to an American might smack of conflict of interest. Twice a year, at mid-summer and yearend, an army of delivery trucks bears such gifts as food, liquor, and soap to people who should be thanked—clients, employers, teachers, landlords. Hiroshi Takaku, an executive at a nonprofit organization, recently spent about \$1,000 on gifts of candy, beer, and canned crabmeat for two dozen people, including his boss, his sons' rugby coaches, and the professor who served as matchmaker for his marriage. To neglect such tribute would be a breach that could sour relations. "It doesn't feel strange at all, it's just social courtesy," Takaku says. "I don't expect anything special."

Nowhere are interests more intertwined than in politics. Indeed, the Japanese have refined back-room dealing to an art. One expression of this is the *zoku*—informal "tribes" of Diet members from the ruling Liberal Democratic Party (LDP) who watch out for different interest groups and intercede deftly when necessary (page 42). In turn, the related industries lavish money on the politicians on a scale rarely seen elsewhere. Japanese experts say it's a rule of thumb, for example, that 2.8% of all construction revenues are funneled to the LDP through its construction *zoku*.

With its enormous clout, the LDP signs off on nearly every penny of the \$3 trillion that Tokyo is spending on public works. And the pork barrel projects are for the power brokers' to dispense. A \$2.6 billion contract for a high-tech magnetic levitation train went to a small corner of the Yamanashi prefecture near Mt. Fuji—the district represented by Shin Kanemaru, chairman of the LDP's dominant faction.

NO FOREIGNERS. As the recent scandals show, collusion is common in Japan. Nowhere is this clearer than in construction bidding. Before the formal bids are submitted for a job, the Japanese contractors meet to decide whose turn it is and what the price should be. One way of quietly signaling bids to others is to write them down on the back of business cards that are exchanged during greetings. Everyone except the pre-agreed winner bids higher. Foreign contractors are not invited to these meetings.

The *zoku* can make or break a foreigner's success in Japan. Washington has been banging on Japan's door for years, complaining that U.S. contractors don't have a fair

...the cellular phone market, to no avail. When Washington threatened sanctions, the issue became a flashpoint in U.S.-Japanese trade relations, and Tokyo relented. Yet the person dispatched to negotiate with the Americans was a high-ranking LDP leader, Ichiro Ozawa. He flew to Washington, checked into a suite at the Watergate hotel, and held a series of grueling meetings with U.S. trade representatives. Along the way, he cut a deal.

NEW HEIGHTS. It's the same old story that underlies the Nomura scandal. After the Plaza Accord of 1985 revalued the world's currencies, Japanese policymakers cast about for ways to preserve competitiveness as the yen began rising sharply. With their hands on every lever of the economy, the bureaucrats were able to set about retooling the system. In short order, excess liquidity was pumped to propel Japan's stock and property prices to unimaginable heights. The Bank of Japan, for example, lowered its key interest rate into the banking system and held interest rates at a low level. Japanese industry was able to raise vast sums of capital cheaply. The result? By 1989, S. Courts of Deutsche Bank in Tokyo estimated that Japanese corporations had borrowed \$100 billion for almost nothing. One result: In 1989, Japanese corporations spent \$660 billion on plant and equipment, speeding past their U.S. competitors, who invested only \$510 billion.

Suddenly, Japan's long-belittled Big Four brokers were star players in their nation's economic plan. Their profits soared, thanks to high fixed commissions sanctioned by the Finance Ministry. The ministry also tolerated *elgyo* (1989), huge funds that brokers were

managing for Japan's blue chips to take advantage of the stock market. Since the scandal, the funds have been banned to cool speculation. When the market crashed in 1990, the brokers felt obligated to cover the losses of their best clients, who helped generate hundreds of millions in profits.

No one challenged the moral soundness of the paybacks. The trouble came because Nomura and others were reporting the payments as tax-

that brokers account for half of all LDP funding.

In the past, the Big Four could easily count on throwing their weight around. When Salomon Brothers & Co. Ltd. in Tokyo became the first foreign broker to introduce a spiffy Wall Street-type bond issue for two Japanese clients, Nomura hit the roof. Nomura officials even charged that Salomon's use of imported financial techniques exposed the Tokyo market

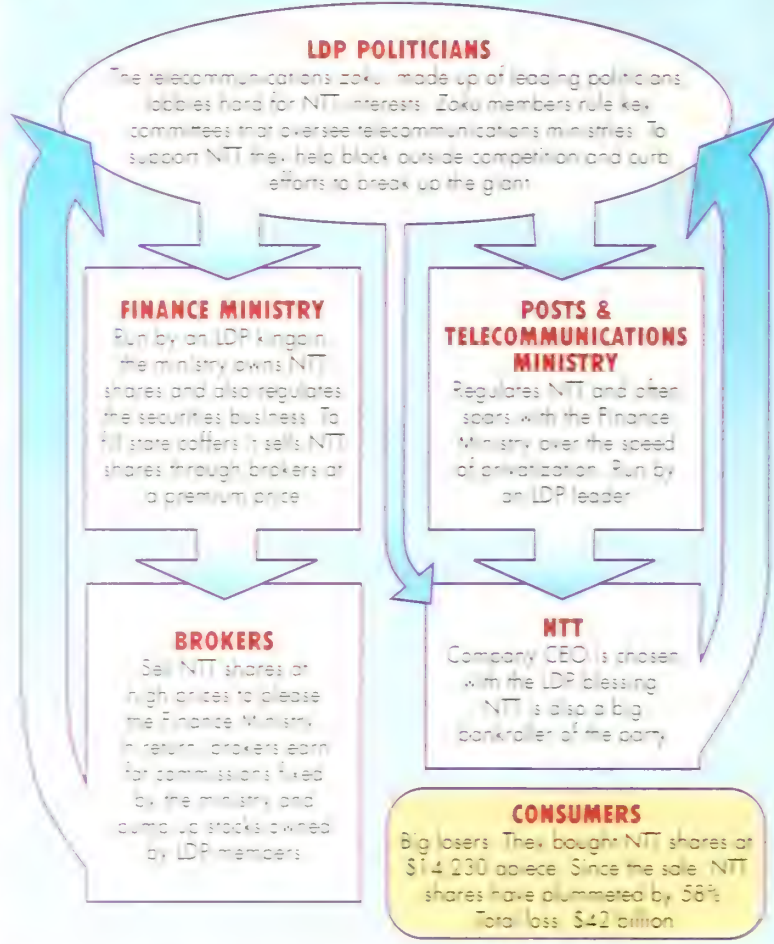
the financial equivalent of AIDS. Salomon now embroiled in its own scandal, watched its two clients back off (page 54).

SKELETONS. But in the battle with the teleshare agency, Nomura overstepped its bounds. Appalled at the broker's arrogance, the officials threw open the floor, exposing closets full of skeletons. No one in Japan could have imagined how vast the scandal would become. Many observers think the loss-compensation scheme would have blown over had it not been for revelations of Nomura's links with the *yakuza*, Japan's Mafia (page 44).

Now the trail is leading to the banks. On Aug. 13, Tokyo was rocked by its biggest bank scandal ever. Some of Japan's most prestigious financial institutions, including giant Industrial Bank of Japan Ltd., were linked to a scheme involving a staggering \$2.5 billion in fraudulently obtained loans. An Osaka restaurant borrowed the money

BEHIND THE NTT SALE

The partial privatization of Japan's telecommunications giant in the late 1980s illustrates the cozy networks linking big business, politicians, and bureaucrats



...the telecommunications expenses. That rankled the Finance Ministry, whose tax inspectors hit the brokers with big bills and penalties. Intoxicated with their newfound status, the brokers resisted and threatened to use their connections with the politicians to beat back the bureaucrats.

Securities heavies often pump up prices of shares held by LDP politicians. Thanks to these hefty "donations," they assumed they had the clout to fend off the ministry. One estimate is

after putting up phony certificates of deposit as collateral.

The Finance Ministry and the Bank of Japan seem determined to press ahead. Aiming to squeeze out the excesses caused by land and stock speculation, officials are cracking down on all kinds of fast-money schemes, from phony certificates of deposit to arbitrage speculation. The moves are swift, taking down high-fliers and even brushing Finance Minister Ryutaro Hashimoto off. It shows the sweeping power the



CHECKING YEN: Japan's power brokers were able to manipulate the economy to generate vast amounts of capital

ry has to shape Japan's economy. In postwar Japan, the Finance Ministry's primary role was to funnel cheap funds to important industries. That was done by keeping interest rates for consumer bank deposits remarkably low, notes Akio Mikuni, who runs his own credit-rating firm. To keep Japan's savings rate high, the ministry levied no taxes on the interest paid to depositors in Japan's massive postal-savings system. "These tax advantages increased the pool of savings and lowered the cost of investment," says economist Jasper J. Koll at S.G. Warburg Securities (Japan) Inc. The Finance Ministry's powers reach much further than those of the U.S. Treasury. Pulling the strings in securities, banking, insurance, and other key industries, the ministry has many of the same functions as the Securities & Exchange Commission, the Federal Reserve, and state banking and insurance regulators combined. The ministry wields more power over Japan's National Tax

Agency than Treasury does over the Internal Revenue Service. And it's the Finance Ministry, not an Office of Management & Budget, that drafts Japan's annual budget.

Enhancing their grip, ministry officials have strictly limited the number of banks and brokers operating in Japan. In the 1950s, the ministry also

seized partial control over the central bank. While the U.S. Fed is completely independent, the Bank of Japan reports to the Finance Ministry.

With so many fiefdoms to run, the ministry exerts its powers idiosyncratically. Its elite corps of officials, almost all of them graduates of Japan's top-ranked Tokyo University, purposely keeps rules vague, forcing bankers and brokers to make frequent visits to its dreary, gray stone headquarters for clarification. In dimly lit corridors and uncarpeted rooms, they wait to be received by one of the 2,000 ministry officials. Control is exercised indirectly, through hints and suggestion, not by American-style regulation. "The fact that the Ministry of Finance can control markets by picking up the phone is an important factor," says Charles S. Stevens, who runs the Tokyo office of the law firm Coudert Brothers.

DOUBLE AGENTS. To stay plugged into the ministry, most banks and brokers offer finance officials senior jobs



ONE OF MANY VICTIMS: Chemist Toshiko Yamamoto watched 60% of her stock portfolio vanish in the Nomura scandal

upon retirement. It's dubbed *amakudari*—or descent from heaven. A recent survey by *Shukan Bunshun* magazine lists 31 former ministry officials in senior spots at securities companies. To a degree, they serve as double agents: They convey their employers' wishes to top Finance Ministry officials and at the same time keep the bureaucrats informed about their company's activities.

This informal control gives the ministry unparalleled clout over the industries it oversees. It is widely accepted that the ministry twisted brokers' arms to prop up the market after Wall Street's Bloody Monday in 1987. Well-informed sources say the ministry pressed institutional investors to continue buying U.S. Treasury bonds despite huge losses. Companies that don't go along know that they'll somehow be penalized later. By prohibiting price competition and new kinds of policies by insurance companies, for example, the ministry thwarts entry by foreign carriers. And the ministry orchestrated a complex scheme, with brokers' help, to privatize telecommunications giant Nippon Telegraph & Telephone Corp. (table, page 36).

Professor Ivan Hall of Gakushuin University in Tokyo sees historical antecedents in the ministry's far-reaching authority. He believes that the legacy of the Tokugawa Era, which ended with the Meiji Restoration of 1868, was that Japan failed to produce a merchant class with political self-confidence to take over, as it did in Western nations (table). Today's bureaucracy is like the old political class in a new guise, the perpetual domination of appointed officials. "It's a Confucian view—leadership by an intelligent elite with the moral obligation to guide the people," Hall says.

CROSSROADS. History might suggest that the ruling power blocs in Japan will never give up ground. But Japan may be at a crossroads as its economy globalizes with a big shift to offshore production. It's no wonder that the organization of the largest companies, the Federation of Economic Organizations, is irate at the brokers for sully Japan's glob-

al image. Gaishi Hiraiwa, the chairman of Keidanren, the big business association, was unusually quick to censure the brokers and to dismiss fired Nomura Chairman Setsuya Tabuchi as vice-chairman of Keidanren. Hiraiwa has also organized a task force on reform.

Indeed, cracks are beginning to show in the "collusive group" running

Japan, says Yoshi Tsurumi, professor of international business at Baruch College in New York. Japanese companies become "borderless," they are eager to move beyond relationship in which the bureaucrats and politicians operate so cozily. To expand internationally, they have to play by global rules, which increasing-

puts them at odds with their own system back home. "The balance is permanently upset," says Tsurumi. "This is the beginning of the end of this cooperative tripartite balance."

By most accounts, that's an optimistic view. The scandals have inspired dozens of proposals to chip away at the Finance Ministry's power and bring the hidden Japan out from the shadows. Some politicians, including Prime Minister Takeshi Kaifu, are calling for U.S.-style oversight agencies. But few reforms are likely to go far. In Tokyo's power corridors the talk is why let an embarrassing episode ruin a formula that works overall?

In the end, there has been only one arrest. Few laws were broken. Those hurt most are Japanese consumers, who wind up paying higher prices for stocks without any safety nets and have little say in what bureaucrats and businessmen decide behind rice-paper screens. But some say the consumers' own attitudes are the problem. Indeed, some Japanese seem almost inured to the kind of under-the-table favors whose disclosure sparked the latest scandals. "It's so much a part of Japanese culture and tradition that the people don't think they're doing anything wrong," says Takeshi Yamamoto, a 34-year-old chemist who watched his stock portfolio plunge by 60% and received no compensation.

Besides, consumers aren't rattled up by this scandal as they were over a 3% consumption tax that passed in spite of unheard-of protests across the country. But as the scandals continue to roil Japan, the world will be learning more and more about what drives the country's success.

By Robert Neff, Ted Holden and Karen Lowry Miller in Tokyo with Joyce Barnathan in New York

A LONG TRADITION OF FAVORS AND BRIBES



SAMURAI WARLORD MINAMOTO YORITOMO CREATED THE FIRST SHOGUNATE NEAR THE END OF THE 12TH CENTURY

THE SHOGUN ERA The Shogun and his samurai despised the merchant class, but needed them to run the economy. To protect themselves, the merchants showered favors on the officials

THE OCCUPATION After World War II, U.S. occupation forces tried to break up the collusion of Japanese politics and big business. They diluted the monopolistic industry groups, organized trade unions, and divvied up landholdings of powerful aristocrats. They even set up a U.S.-type securities oversight agency, which was dismantled when the Americans left

1950s To rebuild the economy, the bureaucrats funneled money into certain industries. New businesses sought political allies, and Diet members coveted their cash. In one case, bribes by shipbuilders to attract the best government loans and contracts ensnared both politicians and bureaucrats in a scandal, including future Prime Minister Eisaku Sato

1970s AND 1980s Desperate for cash to fund expensive elections, LDP politicians accepted bribes and mysterious campaign donations. Exposure toppled Prime Minister Kakuei Tanaka, later arrested for taking bribes from aircraft maker Lockheed. Political reform measures launched by his successor turned out to be toothless. In 1988, the Recruit insider trading scandal implicated nearly the entire ruling party elite

1991 SCANDALS The latest spate of scandals erupted when the bureaucrats took aim at real estate and stock speculators who thrived in the 1980s. To cool Japan's worrisome asset inflation, the bureaucrats turned the screws but with no intention of altering the basic system



Matterhorn

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Manhattan skyline

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***Amoco Procyon:
Changing the course of
the sailing industry.***



Amoco Chemical Company



Innovation from top to bottom, fore to aft, inside and out. The latest materials, combined with the latest technology and design, make the Amoco Procyon the most advanced sloop ever to sail the high seas.

Lightweight Bipod Mast.

This unusual, "upside-down wishbone" is constructed of Thornel® carbon fibers from Amoco Performance Products. Lightweight yet ultrastrong, this material saves about 400 pounds compared to ordinary masts. It's supported by arms attached to the gunwale and can be lowered to travel under bridges.

A unique mainsail furling system and sculptured boom (also constructed of carbon fiber) make it easier to raise and lower sails, cutting the number of crew members needed to two or three.

Thornel was also used to construct the yacht's rudder, and to reinforce the keel and hull.







It began as a notion. A dream, really. A group of ambitious marine designers dreamed of a sailing vessel that would be faster, safer, easier and more enjoyable to sail than ordinary sailing yachts. Using the most advanced materials, they hoped to build something never before attempted: a vessel with the beauty and grace of a sailboat, but with the convenience and

ease of a powerboat. And they would call it Procyon (Pro-see-yon), named for one of the brightest stars in the Canis Minor constellation that has guided sailors safely home for thousands of years.

Now, with the help of Amoco Chemical Company: Amoco Procyon. A 65-foot technological marvel that has become one

20'

10'

87°00'

50'

40'

86°30'



45°00'

50'

40'

44°30'

20'

10'

the brightest spots in a sluggish industry,
paving the way for an entirely new genera-
tion of sailing crafts.
Some of the most striking facts about
Amoco Procyon are:
• It's up to 30% faster than ordinary yachts.
• It requires only a two- or three-person crew.
• It delivers a more comfortable ride be-

cause of induced heaving and better cushioning
comforts both above and below deck.

- It can be ready to sail in just five minutes.

Amoco Procyon would not have been possi-
ble just a few years ago. Just about every inch of
this remarkable craft owes its existence to new
technology and advanced materials produced
by Amoco Chemical Company.



Amoco Chemical
Company

20'

10'

87°00'

50'

40'

86°30'

corrosion-resistant engineering thermoplastic from Amoco Performance Products. It's used in Harken® blocks, winches and steering systems on the boat, allowing for easier sail-raising and rudder-directing and helping to decrease the number of crew members needed for lubrication.

Strong, Lightweight Sails.

P-TA is the chemical intermediate used to make the aramid material (Kevlar®) in Amoco Procyon's tough sails. Amoco Chemical Company is the world's leading supplier of P-TA.

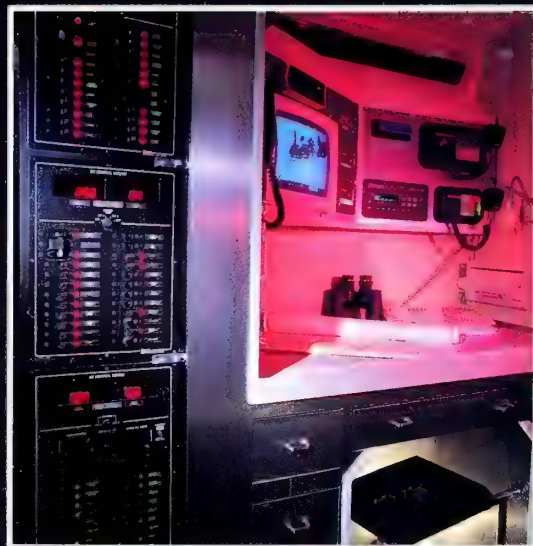
Amoco Procyon's Interior is Elegantly Contemporary, Yet Needs Little Maintenance.

Traditionally, yacht interiors are decorated with old-fashioned materials like teak and brass. While they may be beautiful, they are quite difficult to maintain and require hours of maintenance. So Amoco Procyon is fitted with a number of innovative polyolefin materials from Amoco Fabrics and Fibers Company. Wall coverings, upholstery and carpeting are all made of polypropylene fibers that resist stains, abrasion and fading due to salt and sun damage. Carpeted floors below deck offer surer footing.



Amoco Chemical Company





Unique Canting Keel.

Cast of lead, the keel can automatically cant as much as 25 degrees windward to substantially increase stability and reduce heeling, allowing more sail area for increased speed and comfort.

Sleek, Blister-Resistant Hull.

Research conducted years ago by Amoco led to the discovery that isopolyester laminates are better at blister resistance than orthopolyester laminates. So Amoco Procyon is crafted of an unsaturated polyester laminating resin based on isophthalic acid (IPA) supplied by Amoco Chemical.

Amoco® IPA also plays a major role in the gelcoat applied to the ship's hull and deck, and is the key ingredient in the hull's antifoulant coating. The coating, called Crystic® CopperClad from Ferro Corporation, is composed of finely divided particles of copper suspended in an isophthalate resin that's sprayed onto the hull. Because copper is a natural antifoulant, it is a more environmental-minded alternative to chemical antifoulants.

Hoechst Celanese contributes its product, Trevira® Stoprint™, to the fiber glass in Amoco Procyon's hull. It's based on purified terephthalic acid (PTA) supplied by Amoco Chemical.

And, using Amoco® polybutene, the hull-to-deck joint is sealed water-tight with 8000 Marine Butyl tape from Colorimetric.

Smooth Torlon® Ball & Roller Bearings.

Heading for the Future.

With its innovative bipod mast and canting keel, its creative use of exciting new materials and its stunning yet easy-care interior, the Amoco Procyon is the shining result of combining imagination and technology. Its presence on the sailing scene has enormous implications for the future of yacht manufacturing, perhaps contributing to the rebirth of a U.S. industry that has seen a cut of 50% in new construction since the early 1980s. And none of it would have been possible without quality materials and people from Amoco Chemical.

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JAPAN'S SMALL, SMOKE-FILLED ROOM

A HANDFUL OF MEN CONTROL THE RULING PARTY—AND THE ECONOMY



ALL IN THE FAMILY: Former Ministers Shintaro Abe, Yasuhiro Nakasone, Noboru Takeshita, and Kiichi Miyazawa

One after the other, the limousines pulled up to the exclusive Takemoto restaurant, a favorite nightlife haunt of Japan's power elite in Tokyo's Akasaka district. Out stepped four of the mightiest leaders in Japan's ruling Liberal Democratic Party. Sharing a private tatami-mat room on Aug. 16 were Finance Minister Ryutaro Hashimoto and former LDP General Secretary Ichiro Ozawa, the two top rivals for future control of the party's dominant Takeshita faction, and thus for the office of Prime Minister. Joining them were two even more senior members of the influential faction.

The gathering was prompted by the death the previous day of former For-

eign Minister Shintaro Abe, who had been leader of LDP's second-largest faction. Abe was the consensus pick to succeed Prime Minister Toshiki Kaifu, whose term ends in October. With Abe now gone, the succession was suddenly up for grabs. Whom should former Prime Minister Noboru Takeshita's faction anoint as the next Prime Minister? Takeshita and these four men had the power to decide.

IN SHADOW. The meeting typifies the murky, manipulative world of LDP factions, the quintessence of back-room politics. To understand how the plague of scandals that has wracked Japan this summer might play out, it's necessary to penetrate deep into Japan's political

structure. The LDP's leading factions are not distinguished by issues, or even by commitment to voters. Instead, personal alliances are what count. Interwoven into these factions are the *zoku*, the informal, cross-factional cliques of LDP politicians who serve to protect special-interest groups in return for steady flows of funding (table). With business and politics so tightly interdependent, the climate is ripe for scandal.

As the late-October election for Prime Minister nears, the infighting among LDP factions is pushing the scandals out in the open. Some experts speculate that those hurt most, such as Hashimoto and Nomura Securities Co. former CEO Yoshihisa Tabuchi, hav-

en targeted for leaks because they are close to Takeshita, who was making a comeback after being forced from office in 1988's notorious Recruit scandal. Ironically, the political weakling on whose watch the scandals erupted seems to be gaining the most. As recently as June, hardly anyone gave Kaifu a chance for another term. His lack of clout, so visible internationally, frustrates and even embarrasses many Japanese. His usefulness as a puppet of Takeshita faction bosses—who plucked him from the LDP's weakest sect because they needed a clean, formless face to serve as Prime Minister after a rash of scandals in 1989—seemed near end.

But Kaifu now is the leading contender for the same reason: faction bosses installed him: He's acceptable to the scandal-weary Japanese. He gets high support ratings and can make a strong case that the future of a sweeping program of political reform is pushing rests on his reelection. And Hashimoto, once impetuous as his most likely successor, has been seriously damaged as head of the ministry that is taking most of the blame for the scandals.

Factions aren't unique to Japan, but nowhere are they as institutionalized. Each of the LDP's five main factions has its own formal name, office, budget, and secretariat. They exist because they are the only means for real political competition in Japan. Except for a brief period in the 1950s, the LDP has run Japan since World War II.

The LDP has three groups to bank on for its dominance: Opposition parties, led by the Socialists, have been ineffectual. Big business has been ever ready with its bankroll. And farmers have voted faithfully in return for special treatment. In addition, the LDP has persistently ignored repeated Supreme Court rulings that the current system is unconstitutional.

The key to current faction politics is that nothing can happen without the quiescence of the Takeshita faction. Comprising 106 Diet members, it has 16 more votes than the second-largest Mitsuzuka faction, the former Abe faction now headed by Hiroshi Mitsuzuka. Together, those two allies control more Diet members than do the other three LDP factions.

Traditionally, factional leaders have taken turns running the government by engineering the election of each other as

party president. But the leaders of four of the LDP's five factions today are out of the running. Shin Kanemaru, age 76, of the Takeshita faction, is too old and has never aspired to be Prime Minister. Michio Watanabe, 68, is too coarse and controversial. Former Trade & Industry Minister Mitsuzuka, 64, hasn't sufficiently established himself and is the subject of many scandal-related rumors. And as leader of the smallest faction, Toshio Komoto, 80, is too old and inconsequential.

That leaves Kiichi Miyazawa, 71.

HOW POLITICS AND BUSINESS MIX IN JAPAN

The ruling Liberal Democratic Party is divided into five factions, each with a forceful leader. At the same time, *zoku*, or policy "tribes," run by LDP politicians in the Diet protect business groups, such as agriculture, telecommunications, and construction. In return, the *zoku* receive generous contributions from the industries they support

TAKESHITA FACTION Japan's most powerful political bloc. Named for former Prime Minister Noboru Takeshita, leader of the construction *zoku*, who had to step down after the Recruit scandal. Now run by Shin Kanemaru, telecommunications *zoku* leader. Also includes Finance Minister Ryutaro Hashimoto

MITSUZUKA FACTION Second-largest, headed until May by the late Shintaro Abe, and now run by former Trade & Industry Minister Hiroshi Mitsuzuka. Mitsuzuka belongs to the transportation *zoku* and is regarded as one of the best money conduits in the party

MIYAZAWA FACTION Run by the English-speaking Kiichi Miyazawa, former Finance Minister and member of the finance *zoku*. This faction is Japan's most internationalist in outlook and one of the most dovish

WATANABE FACTION Former Prime Minister Yasuhiro Nakasone's faction now is run by the chatty Michio Watanabe, a powerful leader of both the agriculture and finance *zoku*, and has a hawkish defense orientation

KOMOTO FACTION This smallest of factions has little influence, and Toshio Komoto, a former shipping magnate, funds it out of his own pocket. Prime Minister Toshiki Kaifu belongs to this faction and to the education *zoku*

While neither he nor anyone else is openly campaigning, "he has a very strong desire," says fellow faction member Koichi Kato. Miyazawa, fluent in English, boasts the internationalist skills many Japanese think their country needs. He's more popular with younger members of the Diet than oth-

'Nowadays, politicians devote most of their attention to raising money, not to policy-making'

ers his age. But he was tainted in the Recruit scandal, and his reluctance to play political hardball makes him seem maladroit to many insiders. "He isn't the type to get his hands dirty in a political struggle," says Professor Kenzo Uchida of Tokai University.

In the absence of a clear front-runner, power remains in the hands of the Takeshita group. Continuing to call the shots will be Takeshita, Kanemaru, and, increasingly, the much younger Ozawa. On the rebound from a humiliating LDP defeat in last spring's Tokyo gubernatorial election and a recent heart ailment, Ozawa isn't ready for the top job yet. Many analysts think he will back Kaifu for now. "Kaifu is the easiest person for Ozawa to manipulate," says Takao To-shikawa, chief editor of *Tokyo Insider*, an influential political newsletter.

MONEY TALKS. For most political hopefuls, deciding which faction to join is a matter of political expediency. Koichi Kato's is a fairly typical case. His father was a Lower House member who belonged to the short-lived Fujiyama faction in the 1960s. Seven years after his father died, Foreign Ministry bureaucrat Kato decided to run from the same Yamagata constituency. Since none of the LDP representatives from that district belonged to the Ohira faction, Kato wrangled an introduction to Masayoshi Ohira, who would become Prime Minister in 1978. "I liked Ohira. I wanted to be his disciple," Kato says.

To ensure loyalty, faction bosses maneuver relentlessly to get their members plum jobs. Kato, 52, hasn't done badly. Now in his seventh term, he has served as Director-General of the Defense Agency. And he is widely spoken of as a future

Prime Minister.

Kato downplays the role of money in factional politics, but there's no question it's key. The typical lower House member needs about \$1 million a year to cover such expenses as staff and office rental. But the government only foots 15% to 20% of that bill, enough for two staffers. Yet active, senior Diet members require more like 20 staffers. The average incumbent then needs an additional \$1 million for each election, for which there are no subsidies. "Nowadays," says LDP Diet veteran Masayoshi Ito, "politicians devote most of their attention to raising money, not to policy-making." Anyone who can raise enough money to share with colleagues

ment-oriented groups of LDP Diet members who specialize in such areas as agriculture, telecommunications, and defense. A *zoku's* main function is to protect its particular interest group. Through membership in Diet oversight committees, they intervene with ministries to prevent anything undesirable happening to their business interests. This nexus of bureaucracy, politicians, and interest groups is what Professor Gerald Curtis of Columbia University

With the quid, of course, comes the quo in the form of massive political funding from the interest groups. By some estimates, industry is pumping as much as \$100 million into *zoku* coffers. While most smaller interest groups such as labor unions and consumer groups tend to support the opposition, the LDP's *zoku* look disproportionately to big business and agriculture for funding. That explains why politicians are less than rigorous when it comes to scrutinizing business practices such as those revealed in the latest scandals. This dynamic certainly isn't unknown in the U.S., but laws that are strictly enforced limit how much any member of

Congress can receive from a particular source.

When misdeeds in Japan do come to light, experienced politicians such as Kaifu and Hashimoto are masters at appearing to take public outrage to heart. They will apologize to the voters, exonerate the industry, and promise to take action. Hashimoto may even resign. But don't expect fundamental reform. Even at the grass roots, most Japanese citizens are quick to get over their initial pique. Until a healthy opposition emerges—and that prospect is nowhere in sight—politics in Japan should continue pretty much as usual.

By Robert A. D. in Tokyo

GOODFELLAS, JAPANESE-STYLE: WELL-CONNECTED AND 20% LEGIT

As he holds court in a hotel coffee shop, Shinobu Yoshitsune certainly looks the part of a gang boss. He's stocky; his hair is slicked back, and the tips of his pinkies have been sliced off—the trademark of Japan's *yakuza*, or gangsters. Two underlings hover around him, lighting his cigarettes, paying the bill.

But when Yoshitsune, 34, talks about his 38-member organization, he doesn't seem that different from an ordinary entrepreneur. He operates video stores and real estate and finance companies. He claims that half of his \$1.5 million in annual income comes from legitimate business. He scorns the drug trade. "We're getting to be more like corporations," he says. "We read the business press, and more members are college graduates."

GOLF CLUBS. Indeed, one of the most intriguing revelations of Japan's stock scandal was the web of ties between executives of Japan's top securities firms—Nomura Securities Co. and Nikko Securities Co.—and the *yakuza*. The brokerage executives bought some \$29 million worth of golf club memberships from Susumu Ishii, retired leader of Inagawa-kai, Japan's third-largest *yakuza* family—perhaps to compensate him for losses. The brokerages are also under investigation for ramping up the share price of railroad company Tokyu

Corp., of which Ishii owned 2.9 million shares, possibly to inflate the prices so the mobster could borrow more against them. The firms deny any wrongdoing.

Japanese investigators say the *yakuza* connection with the brokers is part of a broad move into legitimate business. No longer content to confine their activities to businesses at the

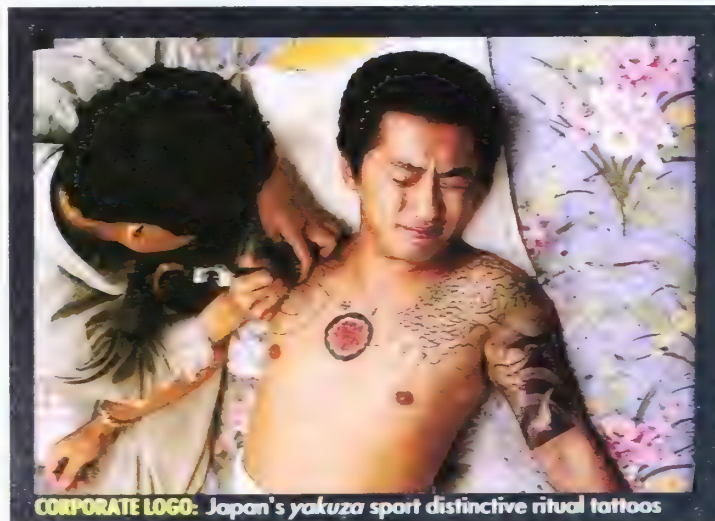
edge of the law, they are now in stocks. Trouble is, police say the *yakuza* aren't always content to let the market take its course. They are said to plant spies in companies to get insider information for stock trades. "They're much more sophisticated now," says Kanehiro Hoshino, a criminologist at the National Research Institute of Police Science.

SELLING SEX. Of course, the *yakuza* haven't abandoned their core businesses. The 90,000 gangsters divided into more than 3,000 gangs control Japan's vast sex industry as well as such other mainstays as debt collection and extortion. A 1990 survey of 3,000 companies revealed that a startling 40 percent paid the mobsters protection money.

As the *yakuza* come out of the closet, the government is starting to take a few shots at them. In May, the Diet passed an antiracketeering law enabling the police to haul in gangsters for trying to strong-arm people by flashing their maimed fingers or distinctive tattoos. The Diet is also likely to take up a money-laundering law in the current session.

But don't worry about the mob's survival. There are strong ties between the *yakuza* and the Establishment that go back at least to the late 1940s, when the gangs were used to keep radical leftists in line. Even now, politicians count on the local gang bosses to get out the votes. "Politicians depend on us for votes, and they do us favors," says *yakuza* boss Yoshitsune. He's confident those lofty connections will help keep the police off *yakuza* backs.

By Karen Lowry Miller in Tokyo



CORPORATE LOGO: Japan's *yakuza* sport distinctive ritual tattoos

markets of society, such as prostitution and gambling, the *yakuza* have been plowing their money into everything from golf courses to land and stocks. Police estimate that 20% of the annual *yakuza* income of \$10 billion is now legit. "They've become deeply embedded in the economy," says Hiroshi Ishizuki, a director of criminal investigation at the National Police Agency.

The stock market is a major parking spot for *yakuza* loot. Brokers say that as much as \$3.6 billion in *yakuza* mon-



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WHY THE HOSTAGE-TAKERS ARE PLAYING 'LET'S MAKE A DEAL'

Lebanon's radical Shiite groups and their Iranian backers are conceding that hostage-taking has failed as a way to squeeze concessions from the West. That acknowledgment is the key to their release of American Edward Tracy and two other Western hostages in early August. Now, as the U.S. seeks to negotiate a grand swap of Western hostages and Arab and Israeli prisoners, the brutal era of hostage politics in the Middle East appears to be nearing an end.

One obstacle to early release of other American captives could be a demand by the radical militias of the Hezbollah militia, which is behind most hostage seizures, for guarantees against U.S. reprisals. Washington is unlikely to give such assurances. But in Lebanon, where 10 Westerners remain captive, the hostage-takers are increasingly isolated. Opposition to them is growing among middle-class Shiite businessmen, who have found themselves hampered in international dealings by being stereotyped as terrorists. "It's commonly recognized in Lebanon, particularly by the Shiites, that holding hostages has not worked," says A. Richard Norton, an expert on the Middle East at West Point.

REALPOLITIK. For George Bush, the captives freed so far are a payoff for his realpolitik approach to the hostage drama, in contrast to the emotional swings of Ronald Reagan and Jimmy Carter. By downplaying the hostages, Bush has lowered their value to their captors. And by warming up ties with Syrian President Hafez al-Assad, despite his harsh rule, Bush has encouraged Assad to turn up the heat on the hostage-takers. Bush also thinks he can keep the pressure on Iran's President Hashemi Rafsanjani to help win the captives' release. Although Iranian radicals in key posts are Hezbollah's primary backers, Rafsanjani is eager for Western investment and

wants a big role in the new Gulf security system that Washington is trying to shape. But he knows the U.S. will be an obstacle to Iranian ambitions until the Americans are freed.

A big gainer from an end to the hostage impasse would be war-torn Lebanon, where Hezbollah militia continue to fight in the South against the Israelis and their puppet South Lebanon Army. As part of any swap, the hostage-takers say Israel must free 375 Arab captives, including Sheik Abdul Karim Obeid, a Shiite leader kidnapped by the Israelis. As a prerequisite for hostage talks, Jerusalem has demanded the return of seven missing Israeli soldiers or an accounting for them. But Israel and Lebanon could both gain from release of the Arab prisoners because it "would remove the *raison d'être* for Hezbollah" in Lebanon, Norton says.

'BUFFER ZONE.' Easing the Lebanon stalemate could also boost prospects for the Mideast peace conference that the U.S. and Soviet Union hope to convene in October. While a breakthrough on the core Arab-Israeli issue of trading land for peace seems unlikely, Syria and Israel could make the conference an early



SYRIA IN BEIRUT: IS A BARGAIN WITH ISRAEL NEXT?

success by agreeing on an Israeli withdrawal from Lebanon in return for security guarantees from Damascus. "You could create in Southern Lebanon an effective buffer zone that would enhance security on both sides," says Brookings Institution Middle East expert William B. Quandt.

The hostage-takers, too, have their eyes on the coming conference. By asking the U.N. to orchestrate a hostage swap, the radicals may be trying to open the way for a bigger U.N. role in the talks than Israel wants. But that is a concession Jerusalem will find hard to refuse if prospects for freedom of the hostages continue to brighten.

By Bill Javetski in Washington and Stanley Reed in New York

GLOBAL WRAPUP

EUROPE

Wrangling in the European Community over the Yugoslav crisis shows that the EC is far from united on an issue as basic as national independence. Major EC members—France, Italy, Britain, and Spain—rejected Germany's proposal to recognize the independence of Croatia and Slovenia. Why? They don't want to encourage other separatists in Eastern Europe—and within their own borders.

With no homegrown separatists to worry about, Germany has exempted Slovenia and Croatia from economic sanctions that the EC levied as pressure to end the strife. This go-it-alone ap-

proach has angered other members. Dutch Foreign Minister Hans van den Broek, the current EC council president, complains that German Foreign Minister Hans-Dietrich Genscher is trying to upstage the EC.

Such squabbling points out how elusive is the EC goal of political union. And some members worry that the Germans, who say they want bigger responsibilities to match their expanded size, are now overreaching.

BRAZIL

A trickle of foreign capital is flowing back to Brazil, encouraged by new Economy Minister Marcilio Marques Moreira's steps to rebuild busi-

ness confidence. In recent months, Brazilian blue-chip companies have been raising money abroad through Eurobonds and commercial paper. At the same time, foreign banks have agreed to take payment in cash and bonds for \$8 billion in overdue interest on Brazil's \$50 billion external bank debt. That paves the way for talks set for Aug. 21 to reschedule debt.

Marques Moreira, Brazil's former envoy to the U.S., is starting to return to Brazilians \$26 billion in bank deposits that President Fernando Collor de Mello froze in 1990 in a drastic attempt to curb inflation. But the \$2 billion monthly payout could give a new boost to prices, which rose 11% in July.

CAT VS. LABOR: HARDHATS, ANYONE?

Caterpillar must cool the UAW before it can fend off Komatsu

Donald V. Fites may well wonder if there's some sort of global conspiracy to trip him up. Just as he settled in as Caterpillar Inc.'s new chief executive last July, Fites faced a cataclysmic economic downturn in Brazil that leveled a \$500 million-a-year market for Cat. Then, the U.S. recession and economic slump in Europe conspired to drive down orders for Cat's array of construction and earth-digging equipment by about 10% this year. In Japan, Cat's joint venture with Mitsubishi Corp. was implicated this summer in an industrial-espionage scandal. And to really put a caper on all of this: Cat is expected to finish 1991 by posting a loss of around \$90 million.

So much for beginner's luck. And if Fites is looking for a breather, he can forget it. Cat's contract with its 17,000 unionized workers, represented by the United Auto Workers, expires on Sept. 30. There's sure to be plenty of head-banging once negotiations start in late August. The sides are far apart on a host of issues, ranging from wages to health care benefits. And Cat's union hands, who have seen their ranks shrink from 40,500, or 58%, since 1979, aren't in a charitable mood. If there isn't a meeting of the minds, odds are union members will take a walk. Warns UAW Local 145 President J.P. Yarbrough: "We won't roll over and play dead."

Neither will Fites. Since the mid-1980s, Cat has been on a worldwide crusade to slash costs and improve productivity in order to stay competitive with arch-rival Komatsu Ltd. In 1987, Cat launched a \$2.1 billion plant-modernization campaign, dubbed "Plant With a Future," to install

more flexible manufacturing capacity. If successful, it could save \$420 million in all by 1993. Last year, in a bid to push more decision-making toward the front lines, Cat eliminated layers of managers and reorganized itself into 17 profit centers. The aim: Slash the company's hefty \$2.2 billion in overhead.

Now, labor is the last frontier in Cat's mission to ensure its survival as a manufacturing powerhouse in the decade ahead. Given the weak dollar against

the yen, Cat's labor costs are roughly the same as Komatsu's. But that could change quickly enough. And says Caterpillar board member John W. Fondahl, a retired Stanford University engineering professor: "There hasn't been sufficient cost reductions there."

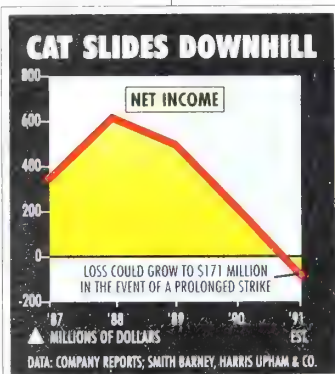
DOCTOR BILLS. It's hard not to admire Cat's cost-cutting zeal. Back in the early 1980s, a bloated Caterpillar ceded market share to Komatsu, which used the strong dollar to storm the U.S. market. Cat's three-year string of losses hit \$38 million in 1984. Humbled, the company cut costs and vigorously pushed exports. Profits reached \$818 million in 1988. Export sales, assisted by a weaker dollar, jumped to \$3.4 billion in 1990 from \$2.1 billion in 1988. More important, since 1986 Cat has regained U.S. market share, climbing to 37% from 35%, while Komatsu has lost about a point to 13%.

Cat veterans have no desire to relive the early 1980s. Cutting labor costs is essential for Cat's pricing competitiveness abroad. "They don't want to rely on the dollar being weak forever," says Tom

bias M. Levkovich, an analyst at Smith Barney, Harris Upham & Co. The UAW contract is an obvious target. Including wages and benefits, the average hourly worker represented by the UAW at Caterpillar earns \$31.74 an hour.

So Fites, who declined to be interviewed for this story, is turning a gimlet eye toward an issue long considered sacrosanct by Cat workers: health care. Cat's strategy is to shift more of the burden of its health care costs to its hourly workers, whose current medical costs are paid in full. Cat's health care costs, including expenses for retirees, run about \$9,000 per active employee. Overall, Cat's health costs rose 14% last year, to \$271 million, and could jump 75% to \$474 million by 1994. The UAW, which protects auto workers' health benefits last year, is expected to vigorously oppose Fites. "We fought 40 years for those benefits," says UAW Local 751 President Larry Soloman.

Other issues could prove just as contentious. Union officials say Cat wants fewer workers protected by job guarantees and hopes to



oid completely the costly income guarantees that auto makers agreed to last year. General Motors Corp. set aside \$4 billion for three years' worth of income guarantees for laid-off workers. Moreover, some union officials suspect Cat wants to push for a two-tier wage system, in which new hires are locked into a lower pay scale.

Fites is playing hardball. During the strike, he launched an advertising campaign in central Illinois, where most of the company's workers live, lecturing locals about the company's need to remain competitive. "Auto industry patterns could not apply to our labor agreements," proclaimed one ad, which went on to tell how high wages and benefits would undermine Caterpillar's fragile recovery. The ads angered the UAW, which got back with an advertising campaign of its own.

And Fites already has insured that the company will keep purring if a strike breaks out. He has built up enough inventory to cover a six-month stretch. That could give Caterpillar the cushion to ride out a long shutdown. Indeed, Fites cleverly gave Cat dealers special incentives and easy payment terms this spring to help them stock up on parts and equipment. With inventory at such high levels, "Caterpillar figures it's a good time to get along with the union," says industry consultant Frank E. Manfredi.

RE SALE. Even so, Cat could face plenty of pain in a strike. Analyst Levkovich believes losses could top \$100 million in the fourth quarter if a strike lasts three months or so. A prolonged strike could slash sales overseas, where inventories are razor thin. Should construction equipment demand pick up in Europe, it may have to swallow the expense of shipping U.S. inventory abroad.

Worse, any extended downtime on the assembly line only pushes back the point at which the financial benefits from Caterpillar's \$2.1 billion plant modernization begin to outweigh its costs. The company already has pushed back the crossover point to late 1992 from late this year.

Even if Fites manages to get concessions without a strike, he still won't be the clear winner. Big inventories mean he will have to slash production by up to 20% in the fourth quarter to bring back balance, say analysts. And since worldwide demand isn't likely to rebound soon, sales may have to start moving machines off the lot at fire-sale prices.

Fites' fans say he's up to the many challenges facing Cat. "He's more forceful than past chiefs," says Fondahl. "Maybe more combative, too." He had better be. His second year on the job promises to be every bit as much fun as his first.

By Kevin Kelly in Chicago



TRAPPED BETWEEN THE UP AND DOWN ESCALATORS

Penney's new image is bringing problems, and profits are sliding

You can hardly fault J. C. Penney Co. for its near-decade-long crusade to refashion itself from a middlebrow mass merchant into a spiffy department-store chain. Retailing, after all, has long been a game tilted either toward low-cost discounters such as Wal-Mart Stores Inc. or to upscale specialists such as Ann Taylor. Penney decided to go uptown: It ditched sporting goods and home appliances while expanding its brand-name clothes, cosmetics, and jewelry. Its once-dreary stores now feature marble floors and fancy woodwork. Consumers took notice: From 1983 to 1989, Penney's earnings nearly doubled, to \$802 million, while revenues jumped 46%, to \$16.1 billion.

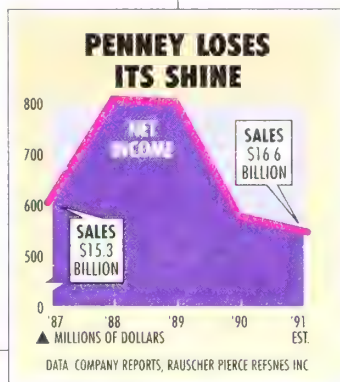
Now, however, Penney's strategy of roping in big spenders has left the retailer in a double bind. While Penney's image has improved since its days as a general retailer, the chain hasn't yet won over the most elite cosmetic and apparel suppliers. Without the carriage-trade goods, Penney just isn't attracting many upper-crust consumers.

Worse yet, tough eco-

nomie times have crimped the aspirations of the kind of upscale-wannabee shoppers Penney had hoped to attract. And the chain's prices are a bit too high for its core middle-class customers. "I used to shop here before they got so fancy," says Nancy Rhodes, a sprightly elderly woman who dropped by a Penney's in Dallas recently—but only to pick up some discounted undergarments.

MARKDOWN TIME. Taken together, these factors help explain why Penney turned in positively dismal quarterly results on Aug. 13. The chain's profits plunged 63%, to \$31 million, while second-quarter retail sales were down 3.5%, to \$3.6 billion. For the year, the 1,300-store chain is expected to post a 5.2% drop in earnings, to \$547 million, on \$16.6 billion in sales, figures Rauscher Pierce Refsnes Inc.

True, the recent recession has creamed a number of retailers. Penney's woes, however, run much deeper. Through the first six months of this year, Penney's same-store sales were off 5.3%, vs. a 0.8% decrease at May Department Stores Co., which also owns Lord &



Toy... at Dayton Hudson Corp.

To halt his company's slide, Penney Chairman William R. Howell is getting out his markdown pen. Prices will be cut on Penney's various private-label offerings. For instance, a Penney's Jacqueline Ferrar women's blazer now goes for about \$89, down from \$135 a few months ago. Howell, 55, also plans to adjust Penney's merchandising mix to attract more recession-weary consumers. And he's trimming capital expenditures from \$600 million to between \$500 million and \$550 million for the year.

Tightening the screws certainly makes sense. But Penney's retreat isn't likely to help it win over more brand-name suppliers, which represent only 35% of the chain's product mix. Sure, Penney has spruced up its men's and children's apparel units with such names as Levi's and OshKosh B'Gosh. But in the key categories of women's apparel and cosmetics—accounting for 42% of total sales—it has had less success.

NO BASKET CASE. Although it recently snagged Revlon Inc.'s prestigious Ultima II line, Penney still doesn't carry Estée Lauder's popular Clinique products. Nor does it offer chic apparel labels such as Liz Claiborne and Evan-Picone. Why? For one thing, this bunch sees little reason to irk existing department store clients—or possibly cannibalize their own sales—by supplying Penney. Says Penney's Marshall Beere, a vice-president in the women's apparel division: "We'd love to have Liz Claiborne, but they're concerned about how much more distribution they can add."

Another issue: Penney hasn't entirely shaken its image as a déclassé retailer. And its visibility among New York fashion houses wasn't helped much by Penney's decision in 1987 to transfer its headquarters from New York to Plano, Tex., where it will move from its temporary digs in Dallas by 1992.

What's more, Penney is still saddled with some recession-sensitive business lines, such as home furnishings, which account for 40% of its catalog and 20% of store revenues. And the housing slump has battered demand for such lines as linens and window coverings, helping to drag down Penney's second-quarter results.

Which is not to say that Penney is a basket case. While debt problems bedevil rival retailers, Penney's debt-to-capital ratio is only 42%, vs. the 59% average for department stores. Yet until Penney is taken more seriously by the Liz Claibornes of the world, it's hard to see how its upscale strategy will ever take hold. Unfortunately, in the status-conscious world of retailing, humble origins are a difficult thing to shake.

By Stephanie Anderson Forest in Dallas

Government

POLITICS

CUOMO'S VOICE IS GETTING LOUDER AND LOUDER

He has a stack of economic ideas. Can he get the Dems to listen?

As the traditional Labor Day campaign kickoff draws near, Democrats are strangely subdued. At clambakes, pig roasts, and state fairs, the bombast of a national campaign is absent, replaced by the whimpers of party officials mulling over a sparse crop of Presidential contenders.

But there's another sound dominating Democratic politics these days, an insistent background buzz that commands attention. "No agenda," it drones, radiating from the general direction of Albany, N.Y. It's a sound that some Democrats find more unsettling than the great stillness gripping the heartland—the sound of Mario Cuomo nagging.

FREE RIDE? No, the three-term New York governor isn't running for President, at least not in the sense of slogging through all those grubby early primaries. Cuomo made that clear in an Aug. 13 interview. "People can speculate all they like," he shrugs. "What I'd like them to do is save a little attention for the merits of my proposals."

Cuomo has them by the truckload. Hesitancy about the nomination hasn't stopped him from showering Democrats with a nonstop stream of unsolicited advice. There is Cuomo, the noncandidate, appearing before the American Stock Exchange on July 25 to call for new investment incentives. There's Cuomo again, at an Aug. 9 mayors' conference in Hyannis, Mass., where he remarked that President Bush is getting a free ride because "right now, the Democrats do not have an agenda for America."

And though no one recalls asking for an encore, Cuomo is taking his "Ask Mario" show on the road. In September, he'll deliver an address in California. The same month, he heads off on a totally non-Presidential trip to Japan. Later in the year, it's on to Europe.

But Cuomo is doing more than touring and talking. He will soon unveil an economic blueprint he hopes will frame his party's 1992 assault on Bush (table). Contents of the document, alternately described as a white paper by Cuomoites and an encyclical by party wags, have been made available to *BUSINESS WEEK*. The report should spark spirited debate:

It represents Cuomo's most detailed exposition yet of an alternative economic policy.

Each feature of the plan, which relies heavily on "targeted" tax breaks and shifts in the tax burden, has been plugged into an econometric model designed by University of Pennsylvania economist Lawrence Klein. Another Cuomo brain trust, DRI/McGraw-Hill economist Lawrence Chimerine, contributed many key ideas. Others who play



THE NONCANDIDATE AT THE AMEX: CRAFTING NATIONAL POSITIONS

ELEMENTS OF CUOMONOMICS

CUT CAPITAL GAINS

To stimulate long-term investment, Cuomo would lower capital gains taxes on assets held for over 5 or 6 years. He may boost the rate on assets held under a year.

TAX THE RICH

Cuomo would hike the top tax rate to 38% vs. 33% now.

HELP THE MIDDLE CLASS

The Governor's Democratic plan: Social Security tax for middle-income Americans. He'd for it by raising the ceiling on wages subject to the tax.

RAISE GASOLINE TAXES

Cuomo may call 20¢-per-gal. gas, raising the levy 5¢ a year for four years.

ninent roles are New York State Economic Development Administration f Vincent Tese and Lee Smith, director of New York's competitiveness committee. Says Smith: "Some Democrats about health or other single issues, taking on the central issue of economic growth, the Governor is filling the democratic vacuum."

Meanwhile, back in "vacuum land" Cuomo's hectoring has begun to wear. Virginia Governor L. Douglas Wilder threw a harpoon Cuomo's way recently when he urged Democrats to ignore pretenders to the throne who preach personal responsibility "but then return to their home states, where they have blighted their citizens with deficit spending." Adds William Galston, a former aide to Walter F. Mondale: "This is realtarting to tick people off. If Cuomo insists to be a one-man Democratic think tank, fine. But unless he gets in the race definitively drops out, his ideas will be drowned out by political speculation." Not all Democrats agree. "If Mario Cuomo offers advice to Democrats,

that's healthy," says top media specialist Frank Greer. "He contributes a lot, even when he's nagging from the sidelines."

Although many wonder why the governor puts so much effort into crafting national positions, Cuomo insists he has been at it for years. He has often issued lengthy tomes on issues from child care to welfare reform. Says Cuomo: "People say 'Oh, this is a campaign,' which it is not. But if that's what it takes to get people to focus on my ideas, terrific."

Cuomo's latest efforts have been framed by New York's fiscal swoon and the belief that Washington has to play a bigger role in capital formation. The result is a policy in sharp contrast to Bush's free-market approach. "The essential fault in Administration economic policy has been the overdependence on encouraging capital investment simply by freeing up wealth in the hands of the wealthy," Cuomo says. "That's supply-side, and it failed."

The centerpiece of Cuomo's plan is a "net investment tax credit." Unlike the old 10% ITC, which cost \$30 billion a

year, the new break would be limited to "productive" investment. "I'm talking about things like pollution-control equipment," Cuomo says. But even a limited ITC tilts heavily toward manufacturing at the expense of services, so the idea may be more nostalgic than effective.

Next, Cuomo, despite railing against the rich, wants to cut the capital-gains tax, now equal to the top income tax rate. He'd phase it down from 33% to 10%. To spark long-term investment, assets would have to be held for five or six years to qualify, while rates would be hiked on assets held under a year.

To complete his role as something of a reverse tax reformer, Cuomo would raise the top tax rate on the wealthy to 38%. And he backs a cut in Social Security payroll taxes to help workers. "It's a very regressive tax," says Chimierine, "and the middle class needs relief."

Some advisers are also urging Cuomo to return to pre-1981 depreciation rules. But he's cautious, saying only that such a costly plan might be phased in. The old system was considered an expensive boondoggle for real estate. Since that's one of New York's comatose industries, Cuomo doesn't seem unduly distressed. "I wouldn't mind a boondoggle for real estate right now," he jokes. "Just a little one."

To help pay for all his tax breaks, Cuomo would junk last year's budget deal. "Terrible," he thunders. He'd convene a bipartisan commission and slash Pentagon spending and entitlement programs. Then he might impose a gasoline tax of 20¢ a gallon, which would encourage energy conservation and ease the deficit. "It doesn't make sense to take the political hit for a nickel," he says.

UNFAZED. He figures his strategy would help boost economic growth from an anemic 0.8% in 1991 to 3% to 3.5%—and release a flood of new revenues. Some economists are dubious. "If you liked the 1970s, you'll love this," scoffs Robert J. Shapiro, of the centrist Progressive Policy Institute. "It's a disturbing collection of tax giveaways from the '70s, and even good ideas like the middle-class tax cut could be washed out by higher gasoline taxes. The key notion seems to be that Washington policymakers can make better decisions than markets."

The criticism doesn't faze Cuomo. Asked whether he is veering away from free markets, he says: "Exactly right. We've had 10 years to show how well the market worked, and we've been shown a \$350 billion deficit and \$3 trillion in debt. Thanks for the lesson." As for pesky questions about '92, Cuomo repeats his "no plans to make plans" mantra and urges: "Forget about me. Remember the message." Sure, Governor. Now about those trips . . .

By Lee Walczak in Albany, N. Y.



ME ENT IT

ants to bring mostly ITC, in 1986, but new assets lucrative" in- s.

U.S. com- ecline in crit- ologies, ould raise R&D tax 30%.

LIBERALIZE DEPRECIATION RULES

Cuomo might try to restore the pre-1981 system of depreciation schedules, which closely tie write-offs to the economic life of plant and equipment.

TRY MANAGED TRADE

Cuomo champions a much tougher U.S. trade stance with Japan and the EC.

FIX THE BUDGET

Cuomo considers last year's budget summit a sham. He'd start over with a bipartisan commission that could recommend sweeping cuts. The Governor envisions big savings in the defense budget and favors means-testing medicare and other entitlement programs, thus denying payments to the well-heeled.

ADOPT AN INDUSTRIAL POLICY

Cuomo dislikes the term "industrial policy," but he favors an activist government role in channeling resources to favored industries. He wants a "national technology policy" to increase government-sponsored R&D and backs expanded job-training programs.

SNIFFING TROUBLE ON SEVENTH AVENUE

The rag trade's factors, who finance the business, are worried

The news flew through the showrooms on Seventh Avenue faster than a changing hemline: Heller Financial Inc., one of the apparel industry's largest factors, had stopped approving orders to Saks Fifth Avenue in late July. When factors—little-known fashion financiers that buy apparel manufacturers' receivables at a discount—refuse to guarantee shipments, they're signaling that they don't trust the store to pay its bills. It's a drastic move that can shut a store down in days: Similar moves by Heller and other factors presaged the bankruptcies of chains such as Federated, Allied, and Carter Hawley Hale.

Of course, Saks didn't shut down. Other factors continued to approve orders, so Saks has weathered the storm for now. But Heller, a subsidiary of Fuji Bank and one of the most conservative factors, remains upset that privately held Saks won't provide more access to financial statements. With the raft of bankruptcies, factors have become the vocal naysayers and referees of the beleaguered retail trade.

'PRESSURIZED.' But if factors can sound the death knell for retailers, the industry's woes are taking their toll on factors, too. Many have been left with millions in unpaid claims from the hordes of retailers that have gone under. And many factors have themselves gone out business. "The environment has become much more pressurized," says Parker Lapp, president of the current asset management group at Heller, where earnings dropped 26% to \$75 million last year. "This past year might rightly be called Operation Retail Storm."

The Heller incident pointed up just how important—and nervous—retail factors have become. For decades, factors toiled as Seventh Avenue's methodical, anonymous bankers, quietly lending money to apparel manufacturers and checking retailers' credit history.

The business may sound simple, but it hasn't been easy lately. Fifteen years ago, 35 to 40 major factors ministered to a burgeoning retail industry. Now, there are fewer than 20. Many of the large, bank-owned factors have gotten out of the business: Chase, Citibank, Bankers Trust, and Chemical Bank have all sold or closed their factoring operations. Bank of New York, which lost \$3 million for the first half of the year, is hoping to sell its BNY Financial Corporation soon.

And the survivors are changing their ways. At Heller, the old litmus test for

approving shipments to a store—"If they pay us on time last month?"—isn't enough. Now, Heller's analysts examine retailers' earnings projections and try to calculate how close the store is to breaching its bank covenants. CIT Group/Factoring, jointly owned by Manufacturers Hanover Corp. and Dai-I Kangyo Bank Ltd. and the industry's largest factor, now has a department devoted solely to checking stores that have gone through leveraged buyouts. Says Francis X. Basile, CIT Factoring chairman: "There's a whole new language of EBIT and EBITDA," or earnings before interest, taxes, depreciation, and amortization, the measurements used to gauge an LBO's vitality.

'OBSCENE.' For some factors, retailing woes are only proof of how much they're needed. "Without bankruptcies we wouldn't be in business," says Joe Heffer, president of Republic Factors Corp., a unit of bank holding company Republic New York Corp. "No one would want guarantees." Chu

Schwartz is one recent convert. As president of Cattive, an upscale women's apparel manufacturer, Schwartz sells over \$10 million worth of merchandise a year to such retailers as Saks and Neiman-Marcus. Until 1988, Schwartz says, he had no problems getting paid and never used a factor. "But from 1988 to 1990, my bad debts were out of control," he says. So this year, Schwartz handed his receivables to Heller Financial.

Not all manufacturers are enamored of factors, though. Bud Konheim, president of Nicole Miller, which sells \$1 million of women's apparel and men's ties annually, guffawed with factors playing the float with his money. "We had occasions where it took 30 days for a factor to deposit check," he says. "That's obscene." Konheim now gets financing from his bank.

Whether factors are the industry's safety net or its usurers, they're certainly its bellwether. They're usually the first to know how retail sales will do the next quarter. And what do they see coming up? "There's a very definite pickup in orders being placed," says Basile. "It may turn out to be a surprisingly good Christmas. But have we seen the last of the big retail bankruptcies? No. So expect the factors' ominous bells to start tolling again one of these days."

By Laura Zinn in New York



CIT'S BASILE: CHECKING STORES MORE CAREFULLY

THE BIG FACTORS IN FACTORING

Factor	Total receivables bought in 1990 Millions of dollars
CIT GROUP/FACTORING	\$6,800
HELLER FINANCIAL	6,500
BNY FINANCIAL	6,200
CITIZENS & SOUTHERN COMMERCIAL	5,800
CONGRESS TALCOTT	4,200
REPUBLIC FACTORS	4,200

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THE SALOMON SHOCKER: HOW BAD WILL IT GET?

Federal investigations into possible T-bond manipulations are rocking the Street and Washington



GUTFREUND ADMITS HE KNEW ABOUT ONE UNAUTHORIZED BID IN APRIL

Some five months ago, Salomon Brothers Inc. relocated from its pale, stone-faced structure at the foot of Lower Manhattan to a building not far away—the never-occupied corporate headquarters of Drexel Burnham Lambert Inc. It was a savvy move in a depressed real estate market, and, at the time, utterly devoid of symbolism. Yet Salomon dominates the supercharged world of U.S. government bond trading almost as completely as Drexel dominated junk bonds. But under Chairman and Chief Executive John H. Gutfreund, Salomon was the embodiment of aggressiveness without aggression—the clean fighter in the velvet glove. When scandal swept the Street, Salomon was untouched, serene.

Today, Salomon Brothers is still the unchallenged king of government bonds. But the storm clouds of wrongdoing that bypassed the firm for so many years have arrived with a thunderclap. On Aug. 9, Salomon issued a gingerly worded statement admitting that it had committed “irregularities and rule violations in connection with its submission of bids in certain auctions of Treasury securities,” that two managing directors had been suspended, and that the bond trading powerhouse was under investigation by the Securities & Exchange Commission and the Antitrust Div. of the Justice Dept. On Aug. 14, Salomon issued an even more detailed mea culpa in which the firm conceded that it failed to promptly take action when it learned of wrongdoing last April and conceded that it may be subject to civil and criminal sanctions, suspended or barred as a broker, or even dropped as a government-appointed bond dealer.

NO SMALL FRY. The question confronting regulators is daunting. Did Salomon deploy vast amounts of capital to manipulate and “corner” the market for government bonds, thereby maintaining its franchise and making illicit profits at the expense of its customers, smaller firms and the bond-buying public?

Just as crucial is the question of executive responsibility. John Gutfreund is

ran trader and a hands-on executive. If, if anything, did he know? And n? Salomon says that management was aware of auction-related misconduct in April—but many Wall Streeters say it may have been a lot earlier. In all, the two managing directors are said by Street sources to have been suspended by Salomon—the firm not confirm their identity—are not all fry. One is Paul Mozer, head of government securities trading desk, the other is his No. 2 man, Thomas phy. Neither could be reached for comment.

Salomon officials would not discuss—the record—the investigation or the firm's trading practices. But the Aug. 14 statement provides damning details, although it raises more questions than it answers. According to the statement, before the auction of two-year Treasury bonds in May, the firm inadvertently failed to disclose that Salomon already had a \$497 million position in two-year bonds, which it had purchased in the "when-issued" market—that is, the market for bonds that have not yet begun trading. "I think a box wasn't checked," maintains a Salomon official.

In other admitted transgressions, bids submitted by Salomon in three earlier auctions, one in December, 1990, and in February, 1991, on behalf of "persons who had not authorized such bids." Salomon then bought back the notes and ended up with 46% of the December auction and 57% of the five-year February auction in violation of Treasury rules. That's a lot more serious than not checking a box—and smacks of a possible attempt to corner the market. Salomon, a Salomon official asserts, the unauthorized bids were nothing more than unauthorized acts by employees. The official emphasizes that higher-level executives—Gutfreund included—had no knowledge of the unauthorized trades.

PRACTICAL JOKE. What would have been the employees' motivation? "I didn't begin to guess," the official replied on Aug. 12. "How these guys thought they could get away with it is on me." But in the statement issued days later, a motivation is given for each of the two February auctions: A managing director was playing a "practical joke" on a Salomon employee. The joke went awry, and the bid which was intended to be submitted was in fact submitted in the name of a customer. "Well, traders and rival bond dealers that corners are no 'practical joke,' rather a commonplace occurrence in Treasury market, and that Salomon committed them in the past—which the firm denies.

But they are divided over the notion that Solly higher-ups would condone a

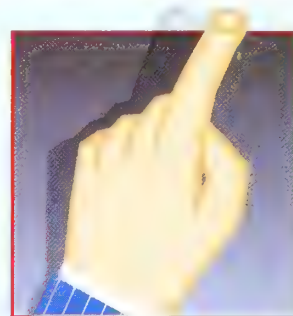
scheme to corner the market. One high official of a rival brokerage fervently believes top management is innocent of wrongdoing. "John Gutfreund and [Salomon President] Tom Strauss and [Salomon Vice-Chairman] John Meriwether had no idea what was going on," he asserts. "I would bet my life on it." Apparently, however, the three top Solly honchos weren't too anxious to do anything when they found out what was going on. The Aug. 14 statement says that Gutfreund, Strauss, and Meriwether were told of one of the unauthorized February bids in April but failed to report it to the government

trader. "Ethics aside, it's embarrassing to do something so simple-minded... if you were going to break the law, you could be more clever."

And sure enough, some traders maintain that Salomon was, indeed, "more clever" for a considerable period of time. They assert that the firm cornered—or "couped" in trading lingo—a number of auctions in a manner that will not be so easy for regulators to prove. "It's been our view for years they've taken the auction down," says one rival trader. "This time they did it more blatantly." Thus the effort to portray top management as a victim of errant employees,

HOW A PRIMARY DEALER COULD CORNER THE GOVERNMENT BOND MARKET

1 The firm puts in a bid for its maximum 35% share of the government bonds being auctioned. To ensure that the bid is accepted, it is made slightly above the going price of the bonds already being quoted in the 'when-issued' market



2 The firm simultaneously puts in a bid, at a similarly high price, for more bonds on behalf of its major customers



3 The bids are accepted by the Treasury Dept.



4 In a prearranged transaction, the firm purchases at cost the bonds it bought on behalf of its customers. When the firm has enough bonds to control the supply, it has 'cornered' the market



5 When other bond dealers want to buy the bonds, perhaps to cover short positions (bonds they sold that they didn't own), the firm can name its price

DATA BW

"due to lack of sufficient attention to the matter."

One of the reasons for the disbelief expressed on the Street is the clumsiness of the machinations confessed by Salomon. "Just a silly thing to do," says Steve Modzelewski, a former Salomon

and negligent at worst, carries little weight with some Wall Streeters and regulators. One senior government official, who requested anonymity, maintains that it is "pretty amazing that top management hasn't resigned over something so blatant happening in a central

operation that they pride themselves on." Suspensions, in his view, might not be enough: "Strong punishment is appropriate here."

The specter of Salomon profiting by abusing Treasury auctions will continue to send shock waves through the Street and Washington. By its willingness to commit huge chunks of capital to the auctions, Salomon provides the liquidity that's vital for the Treasury in its constant replenishment of the government's cash needs. Moreover, the probes are being watched with rapt attention by the thousands of firms throughout the world, large and small, that do business with Salomon. Those firms include virtually every large pension fund, mutual fund, and major financial institution in the country.

Also watching closely are Salomon's rivals in the bond business. Salomon is the most active of the 40 U.S.-authorized primary dealers in government bonds—the brokerages and banks that are the hub of the government securities market. Primary dealers must put in bids at every Treasury auction and either keep the securities or resell them to institutional investors and the public. Among the other large primary dealers are Merrill Lynch and Lehman Brothers, with Goldman Sachs, Morgan Stanley, and First Boston trailing behind. But none can match Salomon in the amount of capital committed to bonds.

LEGAL HEADACHES. Bond trading and bond-sale commissions, largely stemming from its dominance of the government market, are Salomon's main source of profits. So far, Salomon is apparently not losing business as a result of the probe. "Over the years, they have built up a lot of goodwill, and now people will have to wait and see how it happened" before considering a move from Solly, says one money manager in London. But that wait-and-see attitude could vanish if the legal agony mounts. A shareholder class-action suit was filed on Aug. 12, and lawsuits—from bond traders in particular—are but one potential legal headache. A major dealer is actively considering a lawsuit, and a source at his firm says company officials are looking through records to assess what its losses were in the May auction.

But the damage to Salomon's reputation alone may be enough to send customers to the competition, thereby seriously eroding Salomon's franchise and revenue base. "We expect our markets to be on the up-and-up," says Mark S. Venezia, a bond-portfolio manager at the Eaton Vance Management Inc. mutual-fund group. "We have a lot to lose if one premier broker-dealer is guilty of wrongdoing." In foreign markets, where Salo-



STRAUSS (ABOVE) AND MERIWETHER: DID TRADERS ACT WITHOUT THEIR O.K.?



mon has long-established operations, customers are taking a similarly hard look at their relationship with the firm—even if, for now, they are not cutting ties. At Axa, a major French insurance company, international equities manager Jean-Patrick Dubrun is concerned: "It's bothersome when someone thinks that because he's powerful, he doesn't have to obey the rules."

On Wall Street, however, powerful market players have a way of making their own rules—or bending the government's. Traders maintain that the mar-

ket for Treasury notes has been cornered periodically, but only in recent months have they gone public with tales of supposed market-cornering transgressions by Salomon. The brouhaha began in June, when traders publicly complained that Salomon had cornered the May 22 auction of \$12.3 billion in Treasury notes (BW—July 1).

In theory, at least, the mechanics of gaining a corner on the market are terribly sophisticated (chart). The idea is to overcome Treasury rules that set a maximum amount any one bidder can purchase in an auction—35% of a bond or note offering. The head trader at one large bond dealer points out that the first step is to look at the when-issued market.

By bidding just three- to four-hundredths of a percentage point above the price of bonds in the when-issued market, a dealer can be fairly confident the bid will be accepted. Cornering the market is not a solitary pursuit, however, rather a collegial, group enterprise, requiring the cooperation of friendly customers. After all, 35%—the Treasury-imposed limit per firm—does not a corner make. Compliant customers agree to buy the issue at the auction, and then, in general practice, traders say, is to immediately sell their notes or bonds, at a profit, to the dealer. "It's the equivalent of stock-parking," notes an official of one Japanese-owned brokerage.

RIPPLE EFFECT. Cornering the market in this manner is quite different from the transgressions and "practical joke" admitted by Salomon. Under the scenario set forth by traders familiar with the practice, customers are not victims; they are friendly, active participants. "They [Salomon] talk accounts into going along with them," says one trader. "This time, they couldn't get customers to go along with them, so they made them up."

The dangers of cornering a bond short-term note issue are clear. Cornering artificially influence the yield curve—the relationship between long- and short-term interest rates. "How the Treasury yield curve goes affects all bonds, loans, and in some respects, the stock market and the U.S. dollar, too. So anything that happens to the Treasury yield curve ripples through every bond in the country," notes Ron Ryan, president of Ryan Labs, a bond boutique. A more direct effect is that a corner penalizes firms that need to buy the issue—such as dealers who must go short (that is, sell bonds they do not own) in the ordinary course of business. Bonds that are sold short must eventually be replaced, and if one dealer dominates the market it can dictate the price. Indeed, the

SALOMON'S STOCK TAKES A HIT



as the price for every bond buyer. For the dealer, however, a corner is good sense when certain issues of are in short supply. And sure enough, notes Roger Portnoy, an investment strategist with Thomson Financial works, some of the securities that have been in shortest supply are two-year notes—which traders insisted had been deliberately cornered by Salomon. Salomon concedes that the potential legal consequences could be dire indeed. But the firm's status as the top primary dealer is valued by officials of the Treasury and Federal Reserve, who bear the onerous responsibility of financing government on a continuing basis. Some officials say that, as a result, the two agencies will argue against Salomon being severely punished, perhaps depriving the firm of dealer status. But the Justice Dept. and the SEC are likely to take a tougher stance. And the regulators have ample legal tools at their disposal. Although the Securities Act of 1934 does exempt government securities from market manipulation laws, the SEC could pursue charges under Section 10b-5 of the act, its antifraud statute that covers all kinds of misrepresentation. Salomon could also run afoul of record-keeping statutes or be cited for failure to supervise.

BEST CASUALTY. So far, however, Salomon has only begun to feel the pain. Its corners have remained, but the laws have begun. Market participants have lost money in April and May two-year-note auctions are planning to take legal action against Salomon. And if the Justice Dept. throw the book at it by forcing it to disgorge its profits and pay additional damages, the total could wind up at \$200 million to \$500 million in fines and penalties, estimates a lawyer for a potential litigant.

But the biggest casualty may well be Salomon's corporate culture. Despite incidents made in the more genteel investment banking business, Solly is at both a bond house run by and for dealers. Paying traders a percentage of what they earned for the firm gives them an incentive to push the limits, competitors maintain. "The compensation system and greed might have hedged them outside the rules," says a dealer at a competing firm. And the result, notes the top bond trader at another firm, with a touch of hyperbole, is that "every government agency in the world is after them—all at the same time." A sad omen indeed for the firm that replaced Drexel in an office building but never dreamed of taking on the firm's final role—target.

by Gary Weiss, with Leah Nathans-Spiro
by Jeffrey M. Laderman, in New York,
Michael MacNamee and Dean Foust in
Washington, and bureau reports

IS JUNK THE NEW FRONT IN THE WAR ON INSIDER TRADING?

The SEC is probing three firms that invest in sick companies



When Care Enterprises, a nursing-home chain, fell into bankruptcy in March, 1988, its creditors set up a committee to negotiate with management. The committee's co-chair was an executive of R. D. Smith & Co., a New York investment firm and a large Care bondholder. Smith people helped craft a reorganization plan that gave bondholders a big equity stake in the company. Since Care's emergence from Chapter 11 in January, its stock has more than doubled.

But that's not the end of the story. BUSINESS WEEK has learned that the Securities & Exchange Commission is investigating Smith for possible insider trading violations. According to a source close to the probe, the SEC is asking whether Smith used nonpublic data gleaned from creditors' committee negotiations to trade Care's junk bonds. R. D. Smith's general counsel, Kenneth C. Schneier, says the firm made one bond

purchase from another member of the creditors' committee with the committee's and company's knowledge. Otherwise, he says, it "didn't trade. Period."

The inquiry into Smith's trading is just one facet of what is said to be a broad, recently launched probe that represents the SEC's first major attempt to extend the insider trading laws beyond stocks into the \$210 billion junk-bond market. The SEC is also inquiring about possible illegal trading by S. N. Phelps & Co., a Greenwich (Conn.) brokerage firm controlled by Stanford N. Phelps, and Steinhardt Partners, a New York-based hedge fund headed by widely watched investor Michael Steinhardt. An SEC spokesman declined comment.

LOOSELY REGULATED. The agency is focusing on whether bondholders, through membership on creditors' committees or contacts with committee members, have been gleaned inside information. Since these committees negotiate with a com-

pany's management in bankruptcies and out-of-court restructurings, members are privy to confidential data. When the data become public, it often affects the price of the company's securities.

The SEC is said to be asking about the firms' activities in restructurings involving creditors' committees since at least 1985. Schneier says R. D. Smith usually avoids serving on creditors' committees, but when it does serve, it doesn't trade the company's securities. Stanford Phelps says his firm never trades the bonds when it sits on committees or possesses confidential data. Steinhardt partner Gary S. Fragin says suggestions of wrongdoing are "just not true."

The filing of charges by the SEC, while far from certain, could spur a flurry of new investigations and initiatives by the agency to overhaul the loosely regulated debt markets. SEC Chairman Richard C. Breeden has made the high-yield debt market a top priority. Says former SEC general counsel Harvey Pitt: "There's a fair amount of pressure for [the SEC] to come up with something."

Phelps is the best-known firm involved in the inquiry. Stanford Phelps has made a name—as well as millions of dollars—by snapping up a sick company's defaulted bonds and then telling the issuer either to pay the accrued interest on the bonds or face an involuntary bankruptcy petition. His firm has also been active on creditors' committees.

The SEC is said to be asking about numerous deals in which Phelps was involved since the early 1980s. In response to informal SEC inquiries, says Stanford Phelps, the firm has turned over about eight cartons of documents. The SEC, according to a source with knowledge of the probe, has been collecting information on restructurings involving NuCorp Energy, IteL, and Phelps-controlled Citizens Mortgage Investment Trust, now called Citizens Properties. Phelps was not on creditors' committees in these instances, but the SEC is asking whether the firm may have been fed inside data from a committee member. Phelps calls the charge "false."

Steinhardt Partners acquires positions in distressed securities and only occasionally seeks membership on creditors' committees, says partner Fragin. The SEC is expected to explore all deals in which the firm was a member of a creditors' committee. Recent examples were the out-of-court workout of KDI Corp. and the bankruptcy of Insileo Corp. And it is asking whether Steinhardt Partners

may have traded on an illegal tip from someone on a creditors' committee for Eastern Air Lines Inc., which filed for bankruptcy in March, 1989. During this period, the hedge fund accumulated a 6.9% stake in the airline's junior preferred stock. The SEC is said to be studying whether the purchases resulted from inside information on proposed cash infusions or other deals that may have saved Eastern from liquidation. Fragin strongly denies any wrongdoing.

Six-year-old R. D. Smith has been a diversified boutique for investors in troubled companies. It conducts research, invests in the securities of these companies, and recommends them to clients. In looking into Smith's activities as a member of the Care Enterprises creditors' committee, the SEC is believed to be

founder Randall D. Smith sold the firm to some of its key managers. On Sept. 1, R. D. Smith will be renamed BDS Securities Corp. Schneier says plans for changes predated and had nothing to do with the SEC investigation.

For all of the SEC's apparent suspicions, the probe is said to be in its early stages. Typically, before the agency brings charges, private attorneys say it will have to pore through trading records and try to match trades with key events in the negotiations between creditors and management.

UNTESTED AREA. Even if the SEC covers questionable transactions, lawyers add, it may face an uphill battle establishing that trading junk bonds using inside information actually violates the law. Insider trading laws technically cover all securities, but so far they have been applied mostly to stocks. Executives and directors who trade stocks on inside information are usually prosecuted for breaching their fiduciary duty to shareholders. But they owe no such duty to bondholders. Insider traders are also often charged with "misappropriating," or stealing information. Courts haven't applied that theory to junk bonds, either.

The SEC has already set some policies for junk trading by firms involved in reorganizations. In the Federated Department Stores bankruptcy, some bondholders on the creditors' committee sought court permission to trade their bonds. The SEC argued—and the judge agreed—that trading by firms serving on creditors' committees is legitimate so long as the firms set up a Chinese wall between committee members and traders. And

July, a bankruptcy court in Delaware upheld a similar arrangement for bondholders of Harvard Industries. Yet bondholder advisers such as Wilbur Ross of Rothschild Inc. say the SEC should issue much broader ground rules before bringing prosecutions. That way he says, "people who are trying to do the right thing wouldn't have to guess."

Although the law on junk trading is still murky, and questions about trading by Smith, Phelps, and Steinhardt remain to be resolved, the "right thing" is still not exactly an elusive concept. Sooner or later, the SEC will almost certainly establish that junk-bond investors involved in bankruptcies or restructurings should follow one guiding principle: If you want to trade your junk portfolio, stay away from creditors' committees.

By Michele Galen in New York

THE JUNK PROBE

The Securities & Exchange Commission's investigation, says a source with knowledge of the probe, centers on the activities of three investment firms:

S.N. PHELPS

The SEC is asking whether the Greenwich (Conn.) firm used inside information from creditors' committees for aiding companies to trade in the companies' junk bonds. Stanford N. Phelps, the firm's head, denies wrongdoing.

R. D. SMITH

In the 1988 bankruptcy of Care Enterprises, the New York firm co-chaired a creditors' committee that helped craft a reorganization plan. The SEC is asking whether Smith used inside information gleaned from the negotiations to trade Care bonds. Smith says it didn't trade.

STEINHARDT PARTNERS

The SEC is said to be looking into the New York hedge fund's membership on creditors' committees to see if it illegally traded the companies' junk bonds. Steinhardt disputes the charge.

DATA: BW

scrutinizing whether the firm traded the company's debt or tipped off its brokerage arm, which may have bought bonds.

Also said to be under study: whether Smith would routinely collect data as a creditors' committee member, resign from the committee—perhaps because it then would no longer be an insider—and use the data to trade the troubled company's securities. That's how some in the bankruptcy negotiations of utility Public Service Co. of New Hampshire remember it. Says one: "Some people felt Smith was trying to get on the committee for information, got it, and left." Replies Schneier: "With a few exceptions, it's not our policy to get on committees."

Since the SEC contacted R. D. Smith early this year, the firm has undergone a restructuring of its own. In the spring, it trimmed its ranks. In early June,

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AT LAST, THE BIG STORE IS HITTING IT BIG WITH INVESTORS

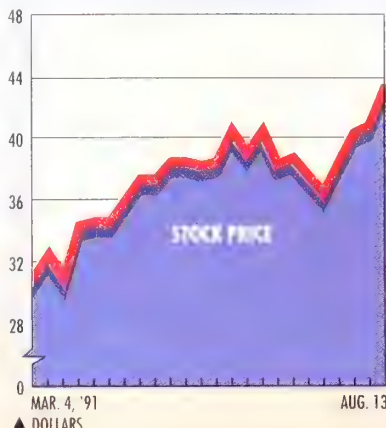
The nation's largest retailer is finally starting to get some respect on the Street. Until recently, Sears Roebuck had been a favorite whipping boy of analysts who saw the company as an also-ran. But now, major value players are buying in. The stock, which traded at 30 in March, has been on the rise, closing at a new annual high of 43 1/4 on Aug. 13.

What's the scoop? Two things: The earnings outlook for the restructured company has turned rosy, prompting some analysts to raise their 1991 earnings estimate. Second, whispers are that a wealthy Asian group has been buying shares with the intention of becoming an influential stakeholder. Says one New York money manager: "My information is that an Asian multibillionaire is behind the group, and the pattern of the stock's recent moves has made me heed the story." This pro declined to reveal the name of the interested mega-investor.

Mark Boyer, whose Boyer Asset Management invests in undervalued asset-rich companies, says Sears has "one of the greatest price-to-intrinsic-value disparities of any large, publicly traded company—certainly of any of the Standard & Poor's 500 stocks." He points out that Sears, with revenues of \$56 billion, ranks as one of the largest corporations in the U.S., with market leadership in most of its businesses. He argues that at its current price, Sears "represents a significant buying opportunity." He puts the company's asset value at nearly \$75 a share.

TURNAROUND TRACK? Here's how Boyer arrives at that price (after adjusting for debt): He values the real estate properties at \$7.3 billion; Allstate Insurance, the nation's second-largest property-liability insurer, at \$7 billion; Sears Merchandising Group, which includes 410 full-line stores and 902 specialty stores, at \$5.3 billion; Discover Card Services, the credit-card folks, at \$3 billion; Dean Witter Financial Services Group, which offers securities brokerage, investment banking, and other financial transactions, at \$1.5 billion; and the Coldwell Banker Real Estate Group, combined with Homart Development, which operates shopping centers, office and commercial

SEARS: HITTING HIGHER GROUND



DATA: BRIDGE INFORMATION SYSTEMS INC.

properties, at \$1.5 billion. Total value: \$25.6 billion, or \$74.61 a share.

After taking some severe cost-cutting steps and introducing specialty-retailing formats, says Boyer, "Sears appears to be on track toward a turnaround." Indeed, the company posted better-than-expected results in the second quarter.

Boyer believes that part of management's agenda is to spin off its real estate and financial-services units "as a way of maximizing shareholder value." Sears declined comment.

QUEUING UP FOR DEALS ON MEALS

It isn't a new television company or another cable TV group. Transmedia Network caters to people who like to eat at fancy restaurants without paying fancy prices. Its charge card offers a 25% savings on meals in some 700 large and small eateries, mainly in Connecticut, Florida, New Jersey, and New York. Recently, the idea has proven appetizing to several money managers. Transmedia shares have jumped to 12 from around 3 in February.

Here's how it works: Using Transmedia's card, which costs members \$50 a year, patrons get 25% off the tab (before taxes and tip) on their Visa or MasterCard bills at participating restaurants. Transmedia advances the restaurant, say, \$5,000 in exchange for credits worth \$10,000 to its card members. The \$10,000 in tabs are returned to Transmedia, which has made \$2,500 on the deal after rebating 25% to the restaurant patrons. The restaurant clears \$1,000, since the cost of food and

beverages usually amounts to only 40% of the gross tab.

Transmedia expects its membership to grow to 100,000 by the end of 1992—double the current number. Business is so good, says one big investor, that he sees sales growing to \$13 million this year, \$23 million in 1992, and \$30 million in 1993, vs. \$7 million last year. Earnings could rise to 50¢ a share this year, 80¢ to 90¢ in 1992, and \$1.25 in 1993, vs. 15¢ in 1990. This pro thinks Transmedia is worth \$24 a share based on its growth potential.

STRONG SIGNALS ON A CELLULAR PLAY

In 1990, when cellular-phone stocks were hot, even the shares of companies only faintly related to the new technology skyrocketed. Nationwide Cellular Service, then a tiny entry with no earnings in sight, raced as high as 14 a share from 2. NCS is now a major reseller of cellular-telephone service and equipment, with revenues that are expected to hit \$115 million in 1992. Yet its stock is stuck at 5 simply because the craze for cellular stocks has cooled.

Not for long, say several analysts. Investor perception may well brighten, since NCS, which has 100,000 subscribers, is expected to break even this year and post its first profit in 1992. "Nationwide is an unappreciated cellular company that will be highly profitable by next year," says Ladenburg Thalmann's Richard Rieger.

As an industry middleman, Nationwide has bypassed the heavy costs of constructing and financing cellular telecommunications facilities that the major telephone companies have had to shoulder. Nationwide obtains cellular services at wholesale rates from the major cellular-system operators. Then it sells these services to subscribers, charging them monthly access and usage fees. It also sells cellular equipment supplied by Japanese and U.S. manufacturers.

That's not all: One big investor says an extra kick should come from one of its divisions—Cellular Technical Services, which went public on Aug. 8 at 4 1/2 a share. Nationwide retained 57% of Cellular, which is expected to earn 50¢ a share next year and \$1 in 1993. Combined with Cellular's income, Nationwide is expected to earn \$1.40 a share next year and \$2.25 in 1993. Based on those numbers, Rieger thinks the stock could double in the next 12 months.

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SURE THE DRUG WORKS. BUT IS IT WORTH IT?

More insurers are insisting on cost-effective products

Cancer sufferers enduring chemotherapy contend with a harsh reality: The potent drugs can so deplete the immune systems of patients that they fall victim to serious, even fatal, infections. So when biotech company Amgen Inc. developed a drug called Neupogen that helps prevent such infections, patients had reason to cheer.

So did medical insurers. A few months after Neupogen was approved by the Food & Drug Administration, a study published in the *New England Journal of Medicine* showed that even though the drug costs about \$1,000 per course of treatment, by preventing an infection it can save roughly \$7,000 in hospital costs. That timely study was no accident. It was part of an Amgen strategy to integrate economic analysis into the process of testing a product's medical effectiveness. And that strategy is becoming one of the hottest topics in drug marketing circles.

'FIRST HURDLE.' Behind the scenes, big drug companies and small biotech businesses alike are scrambling to provide a rigorous analysis of a drug's cost impact long before it hits the market. They're also rushing to prove the worth of existing drugs whose prices are being challenged by third-party payers. With medical costs spiraling, says Paul R. Dawson, vice-president of sales and marketing at Amgen, "economic and health policy research is more important than advertising and promotion."

For decades, that wasn't so. The biggest challenge drugmakers faced was proving that medicines were effective and safe. Once the FDA gave the O.K., companies could charge high prices, and insurers paid up. Who could deny the appeal of a pill or a single injection that could stop an illness in its tracks? That's

how drug companies built the highest profit margins in U.S. industry.

Now, however, the magic is wearing off. As health care costs soar, insurance companies, health maintenance organizations, and government payers are cracking down. Insurers are taking their time agreeing to reimburse the cost of new drugs. And HMOs and cost-strapped hospitals are hesitant to stock these prod-

nies have responded to this pressure. The San Francisco-based Center for Comes Information says the companies are directing their marketers to design so-called outcomes research on the economic and quality-of-life impact of the products. Merck & Co., for example, is funding a trial comparing its blockbuster drug Mevacor, which runs patients about \$700 a year, against other, less expensive cholesterol-lowering therapies. Merck believes the study will show that Mevacor is cheaper in the long run because it works better and has fewer side effects.

It's not as if drugs haven't had to measure up against alternatives before. But manufacturers have sometimes justified huge price premiums based on such factors as whether a drug has to be taken only once a day instead of twice. Now, the studies are including more variables: Does a new drug replace other treatments? Does it have side effects that force the patient to return often to the doctor? Does it actually make the patient feel better? "The FDA may not be interested in this, but the marketplace is mandating this data," notes Gregory K. Tucker, manager of product economics at Hoffmann-La Roche Inc.

TRICKY OUTCOMES. The marketplace also expects outcomes research to be done with the same rigor as trials for the FDA, with the work done by independent, third-party scientists. That's a cry from the "back-of-the-envelope" marketing studies big drug companies historically conducted, says Wayne Roe, chairman of Health Technology Associates, a Washington (D.C.) consultant. Companies would design a small trial to prove a single marketing advantage, such as less stomach upset, and they usually could cancel the trial and quash unflattering findings. "Third-party payers have a much more



ucts until they have proven their value. Even Congress has turned up the heat by challenging the average 20% net profit drugmakers earn on their product lines. Increasingly, "the FDA is only the first hurdle," observes Daniel Paterson, manager of clinical affairs for Access Biotechnology, which helps companies design drug tests.

At least half the major drug compa-

panies have a sophisticated set of ground rules," says David Tennenbaum, director of the medical necessity program for Blue Cross Blue Shield Assn.

Take Group Health Cooperative of Falmouth Sound. The HMO has typically spent 10% of its outpatient drug budget on pain relievers called "nonsteroidal anti-inflammatories," or NSAIDs, mainly to treat arthritis. The cost of these agents

es widely, and there was little information on their long-term effects. An- w Stergachis, a researcher at the rby University of Washington, devel- d a trial to compare arthritis patients n Group Health who had taken four he NSAIDs available. Pfizer makes an ID called Feldene, which costs 12 s as much as the cheapest remedy, is footing the \$150,000 bill for Ster- his' research. Stergachis says he is ducting his research without interfer- . "They are supporting a study, not ing results," he insists.

One problem with the new approach is that some of the potential cost-saving variables are hard to quantify

Outcomes research can be tricky. For thing, some of the potential costing variables are hard to quantify. Gen's anemia-fighter Epogen, for ex- ple, reduces and sometimes elimi- es the need for blood transfusions, etting part of the drug's cost. Hard- o measure is Epogen's value in re- ing the risk of contracting serious d-borne maladies such as hepatitis AIDS from the transfusion. Or in- ply making patients feel better, ch reduces the stress in their domes- ives.

ING FOUL. By the same token, out- es research must not define "cost" narrowly. The University of Missis- i tried to cut its hospital's pharmacy get by eliminating mild sedatives are considered minimally effective. outcome studies later revealed that sicians simply prescribed stronger— more dangerous—sedatives, so the ed-for savings didn't materialize. ntil guidelines are standardized, ie companies will cry foul when their ducts come up short. Genentech Inc. aged to blunt the impact of two e trials that showed that its TPA rt-attack drug, which costs \$2,200 a e, wasn't much more effective than a l costing one-tenth as much. Its sales e persuaded many doctors that those ls had big flaws. ut third-party payers aren't waiting il such tests are perfected. The feder- agency for Health Care Policy & Re- ch is funding outcome studies, and rers such as Blue Cross/Blue Shield pay for better information, too. The hot is that if drug companies can't ve the worth of expensive therapies, r products may never make it to the rmacv shelves.

Joan O'C. Hamilton in San Francisco



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Developments to Watch

EDITED BY ROBERT BUDERI

NO-FAULT ASPHALT MAY SOON HIT THE ROAD



For a nation that worships cars, the U.S. has been remarkably neglectful of its roads. A drive down today's highways presents a relentless stream of potholes, ruts, and lanes closed for resurfacing. The sad fact is that Europeans, with their smooth autobahns and motorways, make stronger roads than Americans do.

But that may soon change. U.S. scientists supported by the National Research Council's Strategic Highway Research Program have made a fundamental discovery about asphalt that could lead to better roads—without the jump in costs it would otherwise take to match European performance. Paving gurus used to picture asphalt as discrete lumps embedded in a sticky gel. But the new findings show that it's more like strands of spaghetti that are bound together and topped with sauce, says SHRP asphalt-program manager Edward Harrigan. With this insight, researchers are recommending asphalt specifications that they hope will avoid problems such as cracking and rutting.

SUPERCONDUCTING MOTORS: GETTING WARMER

Ever since their discovery five years ago, high-temperature superconductors—ceramic oxides that can carry electricity with no resistance at -328°F —have presented researchers with formidable barriers to commercialization. One huge hurdle has been getting superconducting wires to carry the large currents necessary in the workaday world.

In August, these materials took another step closer to the marketplace. CPS Superconductor Corp., a Milford (Mass.) subsidiary of Ceramics Process Systems Corp., announced that its proprietary "melt recrystallization" process is producing wire with "critical current densities" in excess of 100,000 amperes per square centimeter. When coupled with the fact that the wire can still carry nearly half that current in a magnetic field, the materials should be suitable for use in superconducting motors—one of the most important applications. In fact, CPS and Emerson Electric Co. have jointly developed a prototype of a superconducting motor under a grant from the federal Defense Advanced Research Projects Agency. While that's an important step, no one is hinting that a commercial technology is around the corner just yet.

THERE'S MILK-FED VEAL. WHY NOT MANURE-FED HAM?

You could call it the ultimate in recycling: Dutch researchers have found a way to make animal feed from processed manure—and, while they're at it, curb ground-water pollution and reduce acid rain.

One problem with manure is its ammonia content. When manure is spread on fields, much of the ammonia evaporates,

contributing to acid-rain formation. The rest is converted to nitrates, which can seep into the ground and contaminate water supplies. Manure also contains phosphate, another groundwater contaminant that's a common additive in food. Now, Gist-brocades, a biotech company in Delft, Holland, offers a one-two fix: First, specially selected bacteria soak ammonia and turn it into lysine, a protein essential to animal nutrition. It is mixed with pig feed in place of soy. Next, a genetically engineered enzyme called phytase is added to the mixture to help pigs digest phosphorus from plants. That reduces the need for phosphate additives in their feed—a Gist claims the net effect is to cut phosphates in manure 30%. To prove its idea, Gist is setting up a joint venture with a large bank, Rabobank Nederland, and the Dutch commodity board. Commercial manure processing should begin in 1991.

WINDOWS SHOPPING AT THE TOUCH OF A KEYBOARD

Shopping for some new software? Want to know where to get the best deal? You could spend hours squinting at fine-print ads in magazines such as *Computer Shopper* or *Byte*. Or you could stick the *Ultimate Computer Software Buyer's Guide* in your PC, type in a keyword or the desired program's name, and instantly get price comparisons from 40 mail-order houses. For example, the guide lists outlets that offer Microsoft Word for Windows at \$305; elsewhere, you could spend as much as \$349. And the spread for Lotus 1-2-3 (version 2.2) ranges from \$319 to \$395.

Compiled by Lilac Akiko Ltd., a Palm Springs (Calif.) startup, the guide is hardly exhaustive. Last month's edition, for example, lists only 1,300 programs—a fraction of the PC software out there. Still, that's double the number of titles on the inaugural disk in June, and the list keeps growing. If you buy a lot of software, the guide looks like a bargain: \$5 for the latest edition, or \$25 for a six-month subscription.

PUTTING MALARIA BUGS BACK ON THE DEFENSIVE

Malaria ravages the developing world: Across Africa, Asia, and Latin America, some 500 million people suffer from it—and 2 million of them, mainly children, die each year. Things have gotten worse in the past decade, as the malaria parasite has developed resistance to chloroquine, the standard drug used to treat the disease.

Now, Dr. Daniel E. Goldberg of Washington University School of Medicine in St. Louis, Mo., is developing new drugs to tackle the wily bug. It normally invades red blood cells and uses powerful enzymes to devour oxygen-carrying hemoglobin, from which it steals components to fuel attacks on other cells. Goldberg hopes to starve the parasite by blocking the enzymes' ability to chew up hemoglobin. He has identified several promising drugs that mimic a tasty site on the hemoglobin. The enzymes bind to these drugs instead of the hemoglobin and are rendered harmless. Monsanto Co. is helping fund the research, and animal tests could begin in a year.



BY PAUL M. ENG

BETTER VACCINE FOR COMPUTER VIRUSES



Experts have identified about 500 computer viruses—computer codes that can cause PCs to go haywire. There are programs to immunize PCs against known viruses, but new strains, against which PC owners are unprotected, appear every week. Software maker XTree Co. in San Luis Obispo, Calif., says it can help.

The latest version of ViruSafe package has a data base of all known viruses. In that, the program can eliminate recognized viruses residing in a PC's memory or hard drive and spot suspicious-looking codes that could be a new virus. To determine if a code is a virus, ViruSafe creates a temporary file and monitors it the code does to it. If it proves harmful to the test file, ViruSafe adds the new virus to its data base and removes the program from the PC. ViruSafe, itself, is also intended to be immune: It is composed of six overlapping modules, so if one program becomes infected, the damaged portion is deleted and rebuilt from the unaffected five automatically.

PCPY 10th BIRTHDAY, PC AND HASTA LA VISTA

For some people, the 10th birthday of the original IBM PC was cause for celebration—and a chance to mark a decade of amazing growth and technical change. But the Boston Computer Exchange (BCE), a dealer acting as broker between buyers and sellers of used PCs, had other plans: It held a sale, albeit a festive one with wine and cheese. BCE has decided it is time to bury the IBM PC. Trade-in prices for the original PC have dropped from \$2,000 in 1983 to about \$1,000 now. At that price, BCE says it loses money each time it stages a sale. So after Aug. 12, Alex Randall, BCE's president, says his company will bid fond farewell to the original PC and banish it from BCE's trading boards forever. But what to do with your old, no-power, no-frills PC—now that even a used computer broker won't take it? Randall's other organization, East West Education Development Foundation, will gladly take it to institutions that are fostering capitalism in the Third World. Old PCs also make great, albeit very heavy, weights.

SYSTEM 7: YOU READ THE MANUAL, NOW SEE THE MOVIE

Coming soon to a Macintosh screen near you: *System 7—The Movie*. It's an animated cartoon to teach people how to use Apple Computer Inc.'s latest operating system, or core software, called System 7. Unlike previous Mac operating systems, this one can supervise several programs—such as a word processor and a spreadsheet—running at the same time, making it more complex and difficult to learn. To help novices,

the compact-disk-based program uses Aristotle, Leonardo da Vinci, and Sir Isaac Newton as characters to explore various technical aspects of the software. Should viewers have questions regarding material covered by the star-studded cast, Angela, a Mac guru, comes to their aid.

The Whitley Group, a software developer in Charlotte, N. C., originally wrote the training program for use at Westinghouse Electric Corp.'s Savannah River nuclear power station, a large Mac customer. Since then, however, it has begun selling the 45-minute disk to other customers, Apple dealers, user groups, and even Apple Computer itself. *System 7—The Movie* sells for \$150—but buttered popcorn isn't included with the price of admission.

HOW TO GET IBM NETWORKS MOVING IN SYNC

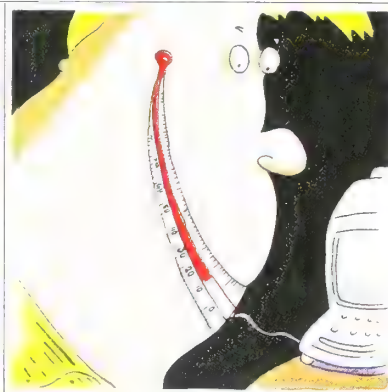
A growing problem for corporations is how to oversee all their personal computers, scattered around offices nationwide—or around the globe. Just making sure machines are using compatible communications or word processing programs can be a big hassle. For instance, the data processing department at headquarters can mail out floppy disks and written orders to install an accounting program update, but there's no way to make sure that every remote office will actually do that when it's supposed to.

Now comes Spectrum Concepts Inc., a New York software company, with a possible solution. Its XCOM/SDS package runs on IBM mainframes and uses their communications networks to distribute software updates to remote PCs and local area network (LAN) server computers. It maintains a central library of PC software on the mainframe, digitally compresses those programs so they'll move faster across the network, installs them on each PC, and provides verification that the installation was successful. Prices start at \$150,000, with deliveries beginning late this year.

TO THIS PROBE, HAPPINESS IS A WARM GUM

On your next visit to the dentist's chair, look over at the tray of tools and you might see something new next to the drill and mirror. Abident Inc. in Danvers, Mass., has come up with a computerized probe that helps dentists detect gum disease. Called PerioTemp, the device measures gum temperature—a measure of inflammation associated with gum disease. Abident developed the system after clinical trials in Boston and Kansas City, Mo., found that temperature was a better indicator of potential trouble spots than bleeding or receding gum lines.

The PerioTemp probe relays the gum temperature around each tooth to a computer monitor, which displays the data with color-coded lights. Red means inflammation, yellow is for borderline spots, and a green light means the gum is healthy. The system, which costs \$1,990, also comes with a printer, so information can be permanently stored in a patient's chart.



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THE SMART STATE FOR BUSINESS

POWER SURGE I HOME PCs

w models and more outlets should buoy Apple, IBM, and Tandy

While back, when sales of pricey personal computers for big businesses began to slip, IBM and Apple Computer Corp. arrived at the same conclusion: Time to jump back into the e-computer market. So the No. 1 and 2 PC makers set up crash programs to design new low-cost models for the Christmas season.

Good thinking. Despite the recession and the conflict in the Persian Gulf, e-PC sales soared. Last summer, market researcher Link Resources Inc. predicted that consumers would spend \$1 billion on home PCs in 1990. Now, it says the total was closer to \$4.9 billion.

There was a hitch, though. The millions of dollars that IBM, Apple, and e-computer perennial Tandy Corp. spent on advertising did drag thousands of consumers into stores. But most of them didn't end up buying those brands. Instead, they opted for IBM clones that, like the IBM Personal System/1, Macintosh Classic, and Tandy 1000 RL, carried price tags starting at \$1,000—only with more power and many more standard features.

LONG START. Even so, IBM and Apple aren't discouraged—or even unhappy. Big Blue got off to a strong start with the PS/1, selling about 100,000 units between its July rollout and the end of the year (chart). Sales started out way above expectations," says Marvin M. Stern, vice president of Sears Brand Central, the division, Roebuck and Co. unit that was among the first to carry the PS/1. IBM consultant Bob Orbach, president of Orbach Inc. in New York City, says: "When it first came out, people really crowded around it in the stores."

Then, sales ground to a halt. Even IBM admits that January and February were terrible months for the PS/1. The company thinks a big part of the problem is the conflict in the Middle East. "Even when we were home watching the war on television," says Skip Gladfelter, marketing manager for IBM's PS/1. Retailers also say that after their surprising success at Christmas, makers of inex-

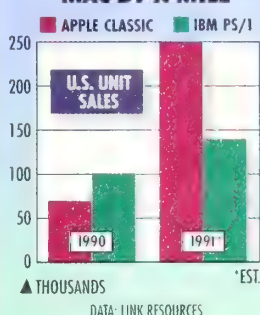
pensive PC clones began focusing more intensely on consumer markets. "As the year progressed, a lot of other manufacturers, such as Packard-Bell and Laser, got very aggressive," says Sears' Stern.

Apple's Classic fared better—once the company was able to ship in volume. Because manufacturing shortfalls limited shipments through Christmas, Link figures Apple sold just 70,000 Classics in 1990. Other analysts say demand was so high for the first low-priced Macintosh that the company could have sold three times that number. Indeed, since then, the Classic has become one of Apple's hottest-selling computers ever. Link says it expects the company to

updated Mac Classic. It will be based on Motorola Inc.'s 68030 processor—a big step up from the current model's 68000 chip, the same type that was used in the original 1984 Macintosh. The price will go up, too: With a hard-disk drive, the machine will list for nearly \$2,000, say dealers.

IBM is planning a power boost, too. Its new PC, dubbed the PS/1½, will use the 80386SX chip instead of the venerable Intel Corp. 80286 processor that powers the PS/1. Dealers say they've been told that IBM hopes to ship the new machine, which will also offer more hard-disk storage than the current model, in October. But they say the company has been

**THE HOME-PC RACE:
MAC BY A MILE**



**BROWSING AT A SEARS
BRAND CENTRAL
IN ARLINGTON, TEX.**



move nearly 250,000 Classics this year.

Now, Apple and IBM are getting ready for another Christmas bonanza. On Oct. 21, when Apple is expected to announce its first notebook computers and some powerful Macs to run computer networks, it is also expected to unveil an

cautioning them about production problems that could cause delays. "If they miss October, they'll be dead in the home-computer water," says one dealer.

Tandy has already updated its home-PC line. In April, it supplemented the badly underpowered 1000 RL with a

home model that uses the 80286 chip, and in August, it added a \$1,299 80486SX-based computer that should go head to head with IBM's PS/1½.

If Big Blue grabs more of the market this year, it will be because it learned from last year's mistakes. The biggest change will be in how its home PCs are sold. When the PS/1 was released a year ago, IBM's strategy called for the machine to be sold through department stores and a handful of traditional PC dealers.

Competition with dealers has forced department stores to slash PS/1 prices and, despite a recent IBM wholesale price cut, margins on the machine are "not what we would wish them to be," says Michael E. Flynn, electronics merchandising manager for Dayton-Hudson Corp.'s department stores. Margins are

If Apple had kept up with demand last year, analysts say it could have sold three times more Mac Classics than it did

higher on a line of Smith-Corona Corp. clones, says Flynn.

In a bid to build sales in the home and small-business markets, IBM and, to a lesser extent, Apple, are moving toward a new category of retailer: warehouse-like computer superstores. These no-frills outlets are emerging as an important distribution channel for consumers and many businesses. Apple just signed up one of the biggest superstores, Comp USA, to carry the Classic and other Macs.

STRAINED RELATIONS? Overall, IBM has greatly expanded its home-computer distribution network. With new superstores and other mass-merchandise retailers such as electronics chains, IBM has tripled the number of nontraditional PC outlets that carry the PS/1 to 2,000. The competition from new discount stores could strain IBM's relations with department stores, however. "We are concerned, to a degree, over the profitability of this line," says Dayton-Hudson's Flynn.

Of course, the weak U.S. economy remains a wild card in this fall's home-computer outlook. This year, Link figures the market will contract a bit, to about \$4.4 billion, because of consumer belt-tightening. On the other hand, if Link's estimates turn out to be as conservative as they were last year, home-computer makers have little to worry about.

By Deidre A. Depke, with Sunita Wadekhi Bhargava in New York and Lois Therrien in Chicago

People

RETAILERS

KAZUO WADA'S ANSWERED PRAYERS

Run by disciples of a small sect, his global Yaohan chain is booming

Kazuo Wada is a devoted diarist, setting aside time each morning to put his thoughts on paper. But his is no ordinary journal. Rather than record the previous day's ups and downs, Wada writes his goals—again and again until he achieves them. "If you write down a goal, it becomes part of your consciousness," explains the deeply religious chairman of retail giant Yaohan International Group. "Then you do it." Wada, 62, has filled 40 volumes with Yaohan goals, and he has accomplished most of them.

These days, Wada's diary has much to say about America. In five years, the Japanese entrepreneur plans to put Yaohan department-store-and-grocery complexes in 20 U.S. cities. He also envisions a nationwide chain of take-out sushi bars, starting with an outlet next year in Manhattan's World Trade Center that'll feature bamboo huts and two sushi-making robots. A listing on the New York Stock Exchange is another top goal. On a visit to Wall Street last summer with a Japanese camera crew in tow, Wada strode up to the exchange building and gave it a hug. Wada's aim is nothing less than to export Japanese culture worldwide. By 1997, he vows, Yaohan will be a \$7 billion empire spanning Asia, Europe, and North America.

DRIED SQUID. At the rate Yaohan stores are proliferating, Wada is well on the way. The son of a Japanese grocer, he has built the family business into an international enterprise with estimated 1991 sales of \$2 billion (table). There are now 117 Yaohan outlets selling Japanese goods around the world, most of them in Japan and Southeast Asia. Eight are in the U.S., and others are going up in Britain, Yaohan's European beachhead, and mainland China. As part of a three-year, \$1.2 billion spending

plan, Yaohan also is expanding worldwide in shoe shops, bakeries, and Chinese restaurants.

In the U.S., Wada is targeting large communities of Asians, who account for at least 70% of Yaohan's U.S. sales. Shoppers at the spacious Yaohan Plaza in Edgewater, N.J., can stock up on pricey delicacies such as dried squid and mundane items such as Japanese brand dishwasher soap, and typical American groceries. They can also arrange reservations at a travel agency, rent Japanese movies, check out the latest in gym equipment, and dine on sushi at a cafe overlooking the Hudson River. The other seven American Yaohans are in California. This year, in hot pursuit of America's fast-growing Asian market, Yaohan is opening megastores in Torrance, Calif., and Chicago. Future sites include Atlanta, Houston, and Washington.

Wada gets his inspiration from a little



an religion called Sei-No Ie, or House of Faith. The sect, which was co-founded by his father when he was a child, combines Shinto, Buddhism, and Christian elements and teaches universal love, positive thinking, and communing with God through meditation. Adherents believe their father has a direct bearing on financial success. Even Yaohan clerks are steeped in Wada's "philosophy of life." Before being hired, applicants must take several months to absorb the "Growth scriptures." Then they write essays relating their philosophy to what jobs they will do. At spiritual training sessions, staff hold hands and tell each other they are beau-

tiful. Employees don't have to join the sect or donate money, but membership seems to be obligatory for managers: They're all disciples. The Yaohan empire began in 1930 as a retail stand run by Wada's parents on a seaside hot springs resort. As a child, Wada was a communist activist who wanted no part of the business. That changed when his mother got him

into the House of Growth in 1951. Adopting the sect as Yaohan's corporate philosophy, he feverishly spread the grocery business and the religion throughout Shizuoka Prefecture. After flops in Latin America, Yaohan hit it big with shopping centers in such places as Kuala Lumpur, Brunei, and blue-collar parts of Hong Kong. The first U.S. store opened in 1979 in Fresno, Calif.

Wada created a stir in 1989—just four months after the massacre at Tiananmen Square—by moving Yaohan's headquarters, as well as his family and personal assets, to Hong Kong. The attraction, he says, was Hong Kong's

WADA'S WORLD

YAOHAN USA

8 grocery/department stores in U.S.; 3 Chinese restaurants

YAOHAN DEPARTMENT STORES

92 department stores/supermarkets in Japan

YAOHAN HONG KONG

4 megastores, with two more under construction

YAOHAN REED

20-unit Chinese restaurant chain in Hong Kong

YAOHAN INTL. CATERERS

Catering outlets, cake shops, Italian shoe factory

OTHER HOLDINGS

17 Yaohan stores in Southeast Asia and Latin America; Malaysian tourist resort

DATA BW

low taxes and hub location in Asia. Wada also wanted to underscore his belief that Beijing won't interfere with high-profile multinationals when it takes over the island nation in 1997. That show of faith, Wada suggests, may have something to do with Beijing letting him bring shopping malls to China next year.

Although Wada speaks neither English nor Chinese, he became an instant celebrity in Hong Kong—a town where money talks. Yaohan spent \$25 million for offices in the top two floors of a waterfront tower and thousands more decorating the interior. Wada himself lives a five-minute walk away in a modest apartment, where he rises at 4 a.m. to pray,

meditate, and write in his diary. Known as a gentle boss who seldom raises his voice, Wada is viewed by his aides as part business genius and part holy man. "He believes that if we have the desire, dreams always come true," says Vice-Chairman Takanori Tsuchiya.

'MISSING THE BOAT'? That outlook will get a severe test in the U.S., where the recession has battered many better-established retailers. While Yaohan's stores have a reputation for good service and are popular with Japanese, analysts say they still aren't profitable. "They're getting better," says Tsuchiya, shrugging. New York retailing consultant Kurt Barnard, a regular customer of the Edgewater mall, thinks Yaohan is "missing the boat" by not marketing to non-Asians. "They're ignoring the tremendous amount of interest in Japanese culture and the more healthful ways Japanese people eat," he says. "Once they break out of that confining shell, they will be immensely profitable."

It's probably just a matter of time, for Wada is nothing if not eager to court Americans. When New York sought money for its June 10 victory parade for the troops, every Japanese company politely declined. When the Japanese Consulate in New York turned to Wada, he promptly kicked in \$100,000. As ticker tape showered upon General H. Norman Schwarzkopf and his troops, Wada gazed proudly down from the VIP booth. Everything was going according to plan. "I will have a big success in New York," he had written in his diary that week. "I will have a big success in New York."

By Pete Engardio in Hong Kong, with Peter Finch in Edgewater, N.J.



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How companies are attempting to clamp down on the after-hours activities of employees



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DRINKERS, DAREDEVILS, AND SMOKERS BEWARE

■ You may not be hired, might even be fired, and could end up paying a monthly penalty if your way of life offends the actuaries

Two years ago, Ford Meter Box in Wabash, Ind., decided it would no longer hire any smokers. Janice Bone was a payroll clerk for the small manufacturer. When a urine test uncovered nicotine traces in Bone's sample, Ford fired her. The incident helped privacy proponents pass an Indiana state law protecting employees who smoke away from work. But Bone, who has filed suit against Ford, has not gotten her job back.

Daniel C. Winn made nearly \$9 an hour setting up machinery at Indianapolis' Best Lock Corp. He was fired after he testified in a relative's legal hearing that he drank socially from

time to time: Best Lock forbids alcohol consumption by employees, even after work. Best also contested his right to receive unemployment benefits, claiming he was fired for cause. A state court ruled Winn eligible, but Best notes that the court didn't hold its "no-drinking" rule invalid.

Do you smoke? Drink? Eat more than you should? Your employer is getting very interested in your answer. It may cost you more in insurance coverage; there's even an off

chance that it could cost you your job. As medical expenses whirl skyward, more companies have begun to see smokers, drinkers, and workers who engage in other "high risk"—but legal—activities as a burden. Johnson & Johnson Health Management Inc. of New Brunswick, N.J., which sells wellness programs to companies, estimates that 15% to 25% of corporate health care costs stem from employees' "unhealthy lifestyle conditions." With health care costs rising a grim 9% each year, employers note, why shouldn't i

lual employees take responsibility their behavior—especially since cor- te health coverage is a perk in the place?

ie employers' concerns are justifi- . Still, they raise a range of ques- s about the employee's right to pri- away from the workplace. So far, a handful of companies have taken extreme stance of Ford Meter or Lock. But many others are institut- disincentives for staffers they deem i-risk—charging them more for th insurance, for example.

isting civil rights laws don't erally protect against "life- e discrimination," because kers and skydivers aren't ed as protected classes. But e 1989, 20 states have passed s banning discrimination nst smokers, and a few give h broader protection (page The backers of such laws are ing a wellspring of senti- t that employers have no ness telling employees how an their private lives, as long hat they do doesn't interfere a how they do their jobs. en they start telling you you t smoke on your own time, next thing you know they'll you you can't have sex but e a week, and if you have sex e a week you're fired," de- es Oklahoma State Senator Franklin, a backer of Okla- a's smoker-protection law.

ER HOURS. Employers have ays had concerns about some hours activities: moonlight- politicking, fraternizing with petitors' employees. But the nological advances and social of the 1980s brought with n a host of workplace privacy es. The result was a new eration of laws and court de- ons spelling out how far an oloyer can go in certain areas. gress has largely banned the

of polygraph testing. The U.S. Su- ne Court has upheld a federal law t prohibits discrimination by federal tractors against persons with com- icable diseases such as AIDS. Ten es have restricted drug testing.

evertheless, some companies contin- to decide what's best for their work- e. For example, Johnson Controls Inc., a Visconsin auto-battery maker, had a y that barred female employees of dbearing age from certain jobs—be- e the exposure to lead in those jobs ht harm any fetus they might con- e. In March, the Supreme Court ck down that policy, ruling that an oloyer's assessment of risks should e substituted for an individual's

own judgment. And plenty of employers still try to enforce their own moral codes when it comes to the sensitive issue of sexual preferences (page 72).

The privacy issue is touching more as- pects of life after hours: everyday activi- ties such as whether you use a seat belt, how much you exercise, and even what sports you like. Multi-Developers Inc., a 100-employee property-development and management company in Georgia, won't employ workers who engage in "hazard- ous activities and pursuits [including]

think we have the right to employ the kind of person we want to have—and that's a nonsmoker," says William M. Shaw, vice-president for administration.

The city of North Miami requires job applicants to sign affidavits certifying they don't smoke, and haven't for a year. Arlene Kurtz, a candidate for a clerk-typist positon, refused to sign and now is suing the city for violation of her right to privacy. Fumes Kurtz (a smok- er): "How can they tell me what to do when I'm at lunch, or in my own home, or over the weekend?" To save on health costs, replies the city's attorney, Pedro P. Echarte: "As a taxpayer, I would like to see my money go into improved schools, roads, and parks, not smoking-related illnesses of gov- ernment employees."

Cracking down on smokers is understandable, because the dan- gers of tobacco are so well-estab- lished. The fear, of course, is that once employers start ques- tioning one type of employee be- havior, the list of unsuitable hab- its will grow. "Why would an employer tell you to knock off smoking at home and not tell you to knock off the beer, if the beer is bad for you, too?" asks Lewis L. Maltby, director of the American Civil Liberties Union National Task Force on Civil Lib- erties in the Work Place. Muses Michael E. Miller, vice-president for administration at Monsanto Co. in St. Louis: "What about the guy who eats fried chicken 20 times a month? I can hear it all coming." In fact, it did come to Athens, Ga. The city government there used to give every job ap- plicant a cholesterol test, elimi- nating candidates whose levels ranked in the highest 20%. Local protest scotched the policy.

It is mainly small businesses that so far are taking broad mea- sures. But not even large em- ployers can ignore the fact that certain habits and health conditions can prove expensive. A four-year study of Control Data Corp. employees found that people with hypertension spent 25% more days in the hospital than those with normal blood pressure and that medical claims of overweight people were 11% higher than those of people who weren't. Smok- ers who work for the state of Kansas spent 69% more time in the hospital than nonsmokers did last year and cost an average \$1,137, vs. \$854 for nonsmokers.

Many companies take a positive ap- proach, in the shape of financial incen- tives that give employees who live right the chance to profit by it. Half of the 22,000 persons covered by Southern Cali-

LIFESTYLE POLICIES: WHAT'S ALLOWED AND WHAT'S NOT

Company	Policy	Started
BAKER HUGHES	\$10 monthly surcharge on health insurance for smokers	1990
EXXON	Employees who have been through rehabilitation for sub- stance abuse can't work in "safe- ty-sensitive" jobs. Workers in these jobs must report any arrest for drug or alcohol offenses	1989
ICM	\$15 a month off medical contri- butions for employees who haven't smoked for 90 days and meet a weight guideline	1991
MULTI- DEVELOPERS	Won't hire anyone engaging in what company views as high- risk activities: skydiving, pilot- ing private aircraft, mountain climbing, motorcycling	1991
TEXAS INSTRUMENTS	\$10 monthly surcharge on health insurance for employees and dependents who smoke	1991
TURNER BROADCASTING	Won't hire smokers	1985
U-HAUL INTERNATIONAL	Biweekly \$5 charge for health insurance for employees who smoke, chew tobacco, or whose weight exceeds guidelines	1990

DATA: BW BUREAUS

such things as skydiving, riding motor- cycles, piloting private aircraft, moun- tain climbing, motor vehicle racing, etc." The impetus for this policy was a very large injury claim the company recently paid. Without this step, Multi-Developers says, coverage for all its employees might have gotten too expensive.

SMOKE-BUSTERS. Already, many employ- ers won't hire smokers. Since 1987, USG Corp., a Chicago building-materials mak- er, has banned smokers from the ranks of 1,200 workers in eight plants. Its con- cern: Smoking might lead to a higher incidence of lung disease among work- ers who work with mineral fiber used in making tile. Turner Broadcasting Sys- tem Inc. won't hire smokers at all. "We

California Edison Co.'s medical plan have reduced their annual premium by \$120 under the corporation's good-health rebate program. They qualify if their weight, cholesterol, and other statistics are within certain bounds. At Atco Properties & Management Inc., a small New York City real estate firm, CEO H. Dale Hemmerdinger pays employees for each pound they lose. And if they walk up the 16 flights of stairs to the office all year, they win a \$500 bonus.

SIN SURCHARGE. But while some companies proffer a carrot, others favor the stick. In a recent Harris Poll for Metropolitan Life Insurance Co., 86% of 1,175 executives surveyed found it "acceptable" to charge higher premiums for unhealthy habits. Since the presence of smokers in a work force drives the group rate up, there is a growing inter-

est in charging smokers more for their insurance—rather than spreading the cost equally among all employees. "Why should we continue to do that when all the medical evidence says smoking leads to health problems?" asks Miller of Monsanto, which is toying with a surcharge.

No reason at all, or so Texas Instruments Inc. figured. This July, spurred by an in-house study showing that smokers' health costs at TI were 50% higher than nonsmokers', the company began charging employees \$10 a month for smoking outside work. The same sum is levied for up to two of the employees' dependents if they smoke, too.

The new charges have prompted no great outcry, perhaps because smokers recognize their puffing is so unpopular. Most of them are bothered, though, that the charge doesn't apply to other habits.

"I think they should go and investigate all types of lifestyles that may increase risk to the company," says a TI programmer who pays \$20 more each month because he and his wife smoke. "Someone who jumps out of airplanes for jollies who races cars on weekends, that could cost the company, too."

Such disincentives will save plenty, enthusiasts say. Oil-field equipment maker Baker Hughes Inc. says its \$10 a month surcharge on smokers has helped reduce the number of employees who call themselves smokers by 7% in the past year (Baker Hughes and other companies generally rely on an honor system to identify smokers.) Its renewal rates for health coverage won't rise at all this year, compared with 20% increases the last four years.

But as much as companies can as-

SMOKERS HAVE RIGHTS—JUST ASK THE TOBACCO COMPANIES

Last spring, a Georgia State Senator introduced into committee a "smokers'-rights" bill outlawing discrimination against people who smoke off the job. In the ensuing week, the lieutenant governor's office got a flood of phone calls supporting the law. So many, in fact, that the phone system broke down.

A strong grass-roots response from the good folk of Georgia? Yes, to some extent. But these complaining constituents got a little help from Philip Morris Cos. When Georgia residents called a toll-free hotline, they heard a recorded message lambasting the lieutenant governor—who was against the bill—for interfering with smokers' rights.

PRAIRIE FIRE? The recording then encouraged callers to "stay on the line—we can connect you to his office right now, toll-free." Hence, the flood of calls. A Philip Morris spokesperson says: "We want to make it easier for consumers to voice their concerns."

The Georgia bill was ultimately withdrawn. But 20 other states have passed similar legislation. Antismoking and health groups warn, however, that these laws are not some "prairie wildfire among state legislators," as Walker P. Merryman, vice-president of the Tobacco Institute, describes them. Rather, they represent a campaign by the deep-pocketed tobacco companies

to counter the antismoking movement. Replies Tobacco Institute spokesman Thomas Lauria: "These bills are put through by the ACLU and the AFL-CIO. The tobacco companies simply help smokers'-rights groups that have already formed."

Early this year, a bill that would prohibit companies from refusing to hire smokers or firing people who smoke

law without his signature in July.

The tobacco companies also target big businesses opposed to smokers' rights bills. Last year, the New York State Legislature passed a broad wording law that would have prohibited companies from forbidding any legal activity off the job. IBM, Eastman Kodak Co., and other businesses wrote strong letters against the bill, arguing

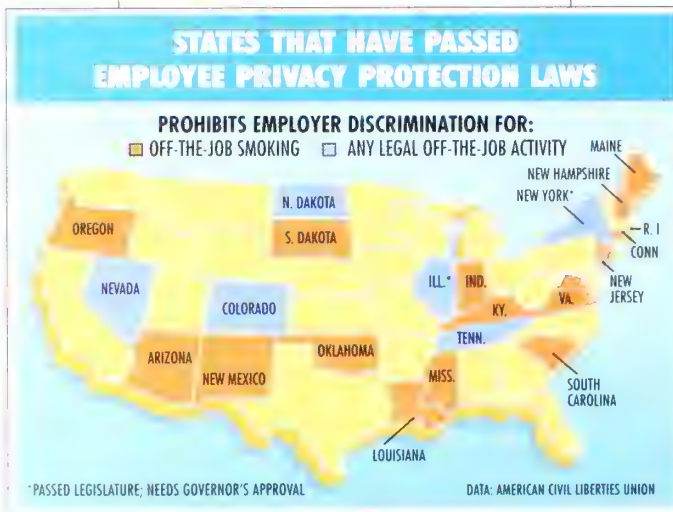
that it would let employees ignore corporate conflict-of-interest policies. Governor Mario M. Cuomo vetoed it.

Now, another version is about to be presented to Cuomo. This time, however, there is no outcry from IBM and Kodak. The reason: Tobacco companies are big buyers of IBM computers and materials for cigarette filters made by Kodak. Rather than risk their accounts, the companies have withdrawn from the debate, say state government officials and sources close to the companies. Neither Kodak nor IBM will comment

on their change of heart, saying only they take no position on the bill.

Surveys show that employees are concerned about employers' legislating their lifestyles. Aware of this, says Joseph Marx of the American Cancer Society: "The tobacco companies are trying to elevate smoking to a civil right"—and taking care of business at the same time.

By Walecia Konrad in Atlanta



was introduced in the state legislature of New Jersey. The tobacco industry hired lobbyists to get lawmakers to vote for the bill. Philip Morris also blanketed the state with support-the-bill letters. R. J. Reynolds Tobacco Co. joined in, using videotapes, sample petitions, and slide shows to help smokers start activist groups. Ultimately, the measure passed the legislature, and the governor allowed it to become

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**GONE
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date unhealthy habits with higher costs, recent research provides little data proving that they can significantly lower costs by inducing employees to change those habits. Although high blood cholesterol is associated with higher health risks and costs, notes Kenneth E. Warner, professor of public-health policy at the University of Michigan at Ann Arbor, "what happens when you lower that? We don't know yet."

MORE CAUTION. Obesity also has been linked to higher incidence of major illnesses and chronic diseases. However, some medical evidence suggests that losing and regaining weight may be more hazardous than being overweight in the first place. In some states, obese individuals have brought—and won—weight-discrimination lawsuits. In 1985, Xerox Corp. had to offer a position, some back pay, and accumulated pension to Catherine McDermott, who was refused a job because of her weight. Xerox claimed that if she were hired, it would have to pay higher disability and life-insurance costs. That argument didn't persuade the court, which held that obesity was a handicap under state law.

Such rulings may become more common when the Americans with Disabilities Act takes effect in 1992. Although it doesn't protect lifestyle behavior *per se*, the act will force more caution in the use of preemployment medical exams. Employers will be able to reject only applicants who can't perform the job. Concern about medical costs won't be a reason for withdrawing a job offer.

These measures are not likely to solve the basic question of how much say an employer should have in an employee's life. Columbia University professor and privacy expert Alan F. Westin worries that if the trend toward lifestyle discrimination persists, employers will eventually hire from a narrow group, "those that are healthiest and cost us less." Eventually, we "could become a two-class society," Westin argues, with "one that is perceived as fit and healthy and the [unhealthy] rest who would be unemployed or marginally employed."

Even if things never get to that point, there's ample evidence that the conflict over workplace privacy is intensifying: As more states pass lifestyle discrimination laws, they provide grounds for legal suits over these issues. Until the verdicts are in, it will be tough both for employers and employees to draw the line between "what's good for business" and "minding your own business."

By Zachary Schiller in Cleveland and Walecia Konrad in Atlanta, with Stephanie Anderson Forest in Dallas and bureau reports

THE RIGHT TO PRIVACY: A \$5.3 MILLION LESSON FOR SHELL?

In many ways, Jeffrey Collins was the very model of a company man—Shell Oil Co., that is. His father retired after 37 years with Shell. Collins spent his entire career there, rising after 19 years to become the No. 2 executive at its Triton Biosciences Inc. unit in Alameda, Calif. But he has spent the past five years suing Shell for wrongful discharge. In June, he won that suit, along with \$5.3 million in damages.

Collins' life with Shell ended abruptly in November, 1985. He had used the office computer to prepare invitations for a nude party planned by his gay sex club. A secretary found one and showed it to company officials. They discharged Collins—wrongfully, a California state judge found. Blasting the company for "outrageous" behavior, Judge Jacqueline Taber held that Shell broke state laws by using information about Collins' personal life as the basis for firing him. "The evidence is clear and convincing that [he] was terminated for private homosexual conduct away from his employment... and not for unsatisfactory job performance," her decision said.

LIFESTYLE QUESTION. Shell, which denies the charges, plans to appeal. A Shell lawyer maintains that Collins was terminated "for preparing a sexually explicit memo" at the office, using company equipment, and "for leaving it where it could offend other employees." The company, which has since sold Triton, denies that it discriminates because of sexual orientation: In fact, it once fired a heterosexual employee for preparing and circulating sexually explicit documents in the office. "We do consider lifestyle characteristics a private matter," the spokesman says.

The Shell case is yet another unsettling reminder to employers of the growing controversy and litigation concerning privacy in the workplace. The Shell judgment "expands the rights of

employees who are being discriminated against because of lifestyle. Employers must make employment decisions on job-related criteria," says Victor Schachter, a prominent employment lawyer in San Francisco who represents several national corporations. Employers certainly will notice the initial size of Collins' award—the largest award yet in a homosexual discrimination case, says Jury Verdict Research Inc.

Indeed, Taber's decision went far in announcing Shell. Not only did she conclude that Collins' dismissal was "solely" because of his homosexuality but she criticized Shell's handling of the termination. To justify Taber held, managers in Alameda and Houston, the company's headquarters, inappropriately to a headhunter of his homosexuality. And she concluded that the termination was



THE COURT SAID SHELL FIRED COLLINS 'SOLELY' BECAUSE HE'S HOMOSEXUAL

an "overreaction" to Collins' mistake leaving the party memo in the office.

Paul F. Wotman, Collins' lawyer, says the Shell verdict "has sent the message throughout Corporate America that being gay isn't an acceptable reason for firing someone." Connecticut, Hawaii, Massachusetts, and Wisconsin—along with some 100 cities and counties—have passed laws protecting gays from bias in housing and employment. No federal law exists, though gay activists have been lobbying since the mid-1970s for a "sexual orientation" amendment to the Civil Rights Act of 1964.

For Collins, 47, redress comes not a minute too soon. Unable to find a job comparable to his \$115,000 position at Triton, he now makes \$25,000 a year at a San Francisco company that ships pets across the U.S. Still, Collins says, hopefully, his court win "will offer a lot of encouragement to people who suffered what I did."

By Maria Shao in San Francisco, with Heidi Dawley in Houston



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The wildflower-filled meadow that came with your house adds a lot to your view and to the quality of life for everyone who passes. You'd like the scene to be there forever. But property taxes keep going up, and even if you never sell to a developer, your offspring might.

There is a way to preserve the pastoral scene and probably get a tax break, too: by locking away that prized parcel in a land trust. It's a lot like turning over your stock portfolio to a trust. You can reap the benefits, but the trust will be there to guard

the assets—in this case, the land—long after you're gone.

Basically, a land trust is a nonprofit corporation, registered with the Internal Revenue Service as a 501(c)(3) organization. This status allows you to get a charitable tax deduction for the land you donate. You can set up your own trust, preferably with the help of a lawyer experienced in this area. Or you can work with one of the many regional or national organizations that have sprung up in recent years (table).

The simplest way to use a land trust is to donate your property to it and take a de-

duction for the fair market value. To convince the IRS that you're not overstating the value, you must obtain an independent appraisal. Draw up a "very, very realistic" subdivision plan to show what the land would be worth to a developer, advises Patricia Pregmon, an attorney with Duane, Morris & Heckscher in Philadelphia.

LIMITED USE. Instead of donating their land outright, many people give or sell a "conservation easement" to a land trust. With any easement, you forfeit some of the rights that come with owning land; a common form of easement,

for instance, allows a utility to run power lines across the property. In the case of a conservation easement, a deed restriction typically declares that the property can never be developed, not by you or anyone who owns it in the future. One posthumous advantage is that "it can keep you heirs from fighting" over how to handle the land, notes Andrew Johnson, president of the Conservation Advisory consulting firm in Chad, Ford, Pa.

But the easement does have to lock away all your real estate. Many people give up development rights to or

of their property, keep some acreage available for future sale and thus gain economic peace of mind," Steven Rosenberg, land preservation director of Scedudson, a Poughkeepsie environmental group, is committed to protecting the Hudson River. But donating an easement brings a much greater income-tax break than selling land outright, and is less likely to wring any property-tax relief from your assessor.

IL POLLUTION. In fact, it could end up boosting your property-tax bill, but in a nice way. While the market value of protected land plunges, the guarantee of open space enhances the value of boring properties," says Morris, a leader in Pennsylvania's French & Ring Creeks Conservancy Trust in Pottstown, Pa. In 1967, it has arranged space easements on 3,800 acres in a path of development north and west of Philadelphia and has succeeded in preserving his buildings and creating

ed the idea of seeing the place spoiled by "visual pollution." So Heaton and a few neighbors formed the Willowemoc Land Conservancy.

Instead of acquiring land or banning development, they came up with an agreement setting rules that each neighbor has the right to enforce in court. Among them are that satellite dishes must be black mesh instead of white. Houses must be in earth-tone colors and located at least 200 feet from the creek. This purely local approach, he says, "is a source of satisfaction and visual value to everyone involved."

No matter how simple they're meant to be, conservation easements have to be drafted carefully if they're to stand up in court, in the eyes of the IRS, and even to the forces of nature. Often, the easement specifies an organization that can go to court against anyone who might violate its terms.

NO LOOPHOLES. More complicated arrangements, such as a will instructing the executor of your estate to create a conservation easement, need airtight language to keep disappointed heirs from a court challenge. If it's a "recreational" conservation easement, you might have to provide for public access to satisfy the IRS. Public access isn't likely

to be required, though, if your easement specifies another conservation purpose, such as protecting significant habitat for wildlife.

If you want your meadow to remain a meadow forever, you might need to provide for a caretaker to maintain the property. "Perpetuity is a long time," says Erik Axelsson, a Philadelphia-based Nature Conservancy staffer. Left alone, he points out, an abandoned farm can revert to forest in just 50 years. And unless you protect it with such weapons as a trust or conservation easement, it can turn into a subdivision even faster.

Dick Janssen

Smart Money

EASING THE BITE OF JUMBO MORTGAGES

With real estate prices at their lowest level in years, now is a good time to scout out a deal on a dream house. But if you need to borrow more than the \$191,200 limit set by most banks for conventional fixed-rate mortgages, the cost can be prohibitive, even with today's low mortgage rates. So-called jumbo mortgages typically carry interest rates half a percentage point higher than conventional loans.

Recently, a handful of lenders, including Merrill Lynch, Bankers Trust, and Boston Safe Deposit & Trust, have started offering an alternative: prime-rate-based jumbos. These loans offer two advantages over regular jumbos. Their rates are pegged to the interest rate that banks charge for business loans—currently 8.5%. And 100% of the payments you make in the first 10 years is tax-deductible interest.

BETTER RATIOS. At today's prime rate, monthly payments on a \$350,000 prime-based mortgage are \$2,479, a savings of \$464 over a conventional fixed-rate jumbo's 9.5%. You could save as much as \$12,566 during the first 12 months if, say, the regular jumbo carried two points and the prime-based jumbo was point-free, as is often the case. Amortization of principal doesn't begin until the 11th year (though you have the option of prepaying the principal). With a regular \$350,000 jumbo, on the other hand, 94% of the first year's payments would go toward interest and 6% toward principal. The ratio would be

91%/9% in year 5 and 86%/14% in year 10.

There is a catch. Prime-rate loans are aimed at six-figure earners who have substantial investments outside real estate. Some lenders also prefer customers who have enough assets to be able to pay off the loan

TWO WAYS TO PAY OFF A \$350,000 HOME LOAN

	Prime jumbo	Fixed-rate jumbo
INTEREST RATE	8.5%	9.5%
POINTS	0	\$7,000*
MONTHLY PAYMENT	\$2,479	\$2,943
FIRST-YEAR PAYMENTS**	\$29,750	\$35,316

*Two points

**Not including points

DATA: BOSTON SAFE DEPOSIT & TRUST CO.

quickly if the economy takes a dive. Lenders want that assurance because prime-based loans are variable, with monthly payments changing every six months to follow the prime. Since 1986, the index used for these loans has floated between 10.5% and 7.5%. But in 1981, the prime soared to 20%. If something similar occurs, bankers don't want to get burned by borrowers who can't repay.

Many borrowers prefer the predictability of a fixed-rate loan, says Cary Geller, an accountant with Tofias Fleishman Shapiro financial planners in Cambridge, Mass. But "at the high end of the market," says Geller, "it's hard to find a competitive fixed-rate product."

Prime-based jumbos may be ideal for those who need only a short-term mortgage and want to maximize tax savings. They might also appeal to borrowers who want to refinance high-interest, fixed-rate mortgages. Either way, it takes some of the sting out of the cost of that dream house. Geoff Smith

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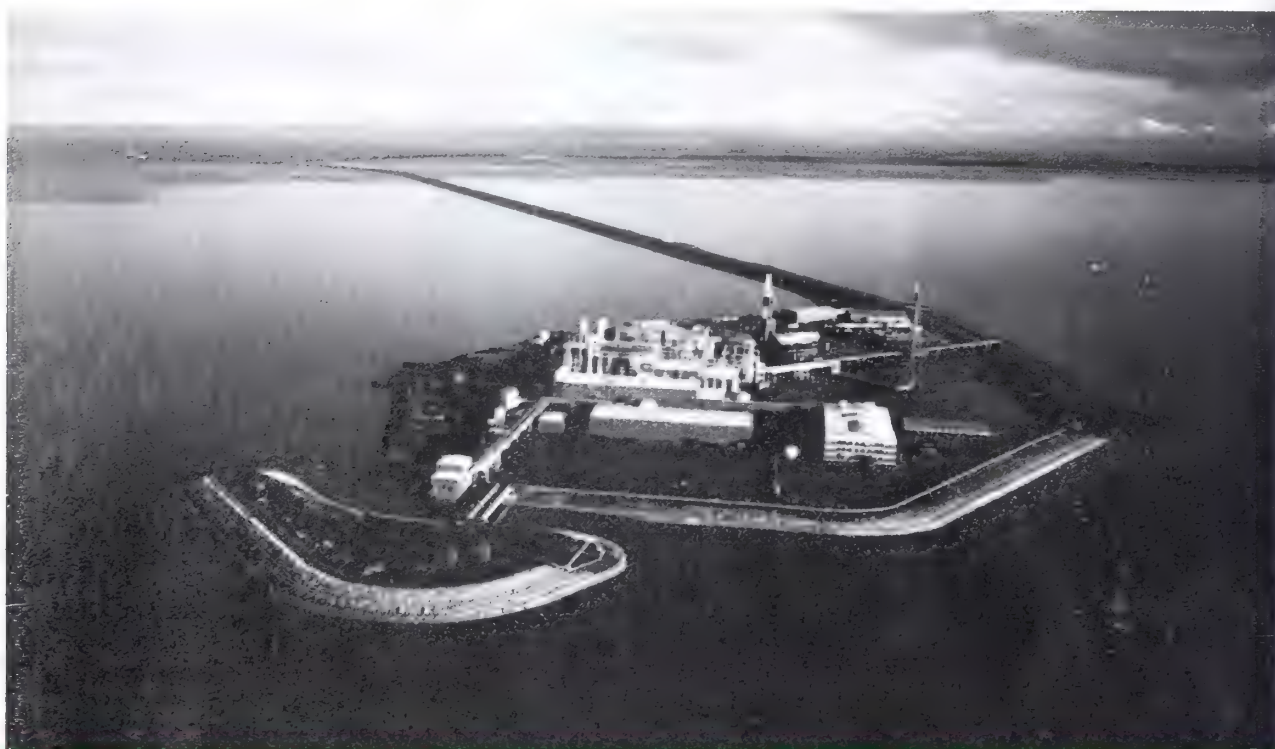
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Calif. 94105, 415 495-4014

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hiking trails and a nature center. Not all efforts are so elaborate. Having bought the shell of an old house on "112 beautiful" in upstate New York, Bert Heaton put in a lot of "pulling mattresses out of blackberries" and hat-

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The Energy To Change



Food

WHERE CITY SLICKERS CAN FIND DOWN-HOME BARBECUE

ew American foods incite such passion and hyperbole as barbecue. Fans have devoted books to the fine points of cooking over a wood fire. Barbecue is feuded fiercely over the meats and cuts to use or pork, shoulders or

Formica tables, and fuming pits out back—aren't the only places to get the ribs of your dreams. You can find barbecue bliss in big cities—or even pick up the phone and have it delivered to your door. Many good places now ship, includ-

logs. Doug Keyes, once a Texas cowboy who cooked barbecue at rodeos for the likes of Roy Rogers and Gene Autry, says his wonderful sauce contains plenty of ginger, a little vanilla, plus "some things I don't let nobody know." Carson's Ribs, with five locations around Chicago, charges \$12 a slab plus shipping.

Then there are some shrines of smoke you'll just have to visit, since they don't

Highway in Miami. But many places require more. Also, be prepared for rustic decor and no air-conditioning. Inside Shorty's rough-hewn log exterior, there are rows of picnic tables on a cement floor. Mounted on the wall are a boar's head, a water buffalo's head, and a deer's rear end.

One point to remember: Don't even think of asking for the reci-



BARBECUE BY MAIL

Name/Location	Phone number	Description
SON'S RIBS Chicago	312 275-5000	\$12 for a slab of baby back beef ribs, plus shipping
CHARLIE VERGOS' RENDEZVOUS Memphis	800 827-RIBS	\$85 for minimum 5 orders of pork ribs; with sauce and special spices*
DOUG'S BAR-B-Q Emeryville, Calif.	415 655-9048	\$15 for a slab of beef ribs; \$30 for a turkey, plus shipping
MAURICE'S BAR-B-Q San Francisco	800 MAURICE	\$49.95 for three pounds chopped ham in mustard sauce*

*Includes shipping costs

DATA: BW

the wood that produces most flavorful smoke (hickory, oak, or pecan), and long to cook (at least 8 to 10 hours over a low fire, pur-

say). And everybody has a favorite BBQ joint. "When I die," says five-star chef Dean Fearing, a devotee of Sonny Bryan's Smokehouse in Dallas, "I want to be face down with a rib in one hand and a Lone Star in the other."

W-A-S-LAB. Rural areas in the Deep South—think of country lean-tos with screen doors, chipped

ing Charlie Vergos' Rendezvous in Memphis, Carson's Ribs in Chicago, and Doug's Bar-B-Q near San Francisco (table).

The Rendezvous is a Memphis institution that cooks meat "dry" in a vinegar base, which leaves it tender, not sticky from sauce. It ships frozen barbecued pork ribs and shoulder overnight. The Vergos family also offers tomato-based sauce on the side.

Doug's Bar-B-Q at 3600 San Pablo Ave. in Emeryville, Calif., charges \$15 a slab plus shipping or \$30 for a whole turkey grilled over black oak

deliver. They'll hit you with the sweet smell of woodsmoke before you go through the door.

Among the most famous is Arthur Bryant's at 1727 Brooklyn St. in Kansas City, Mo. The founder called it "the grease house." But don't let that scare you. Bryant's heavenly sauce inspired writer Calvin Trillin of *The New Yorker* to hail it as the world's best barbecue. Bryant's, like many great places, is jammed, and plain as linoleum; you may want to carry out.

SPLATTER FACTOR. Houston's Goode Co. Texas Barbeque is also famous. The original chow house at 5109 Kirby Dr. is crammed with Texana ranging from steer heads to rodeo posters, and a bigger place at 8911 Katy Freeway resembles a 19th century dance hall. Locals rave about the mesquite-smoked brisket, jalapeño cheese bread, and pecan pie.

Wherever you go, dress for the splatter factor, since you eat with your hands. Our correspondent got through dinner with only four napkins at Shorty's B-B-Q, 9200 S. Dixie

pe of your favorite sauce. We tried with Edith Colston of Edith's Bar-B-Q at 1836 N. Clybourn Ave. in Chicago. Since 1970, she has been serving up what some say are the best ribs in the city—delicate, meaty, and cooked over hickory. But Edith gets downright protective about her recipe. "Nobody gets that," she swears. "That's mine till I finally go."

Julie Siler

Worth Noting

■ **POLICE YOURSELF.** Community's handheld breathalyzer tells whether you're fit to drive after drinking. The \$200 device weighs eight ounces and fits in a glove compartment. For information, call 800 637-8363.

■ **SAFE WORK.** A new Labor Dept. booklet, *Ergonomics: The Study of Work*, examines work patterns that can cause repetitive-motion and other physical disorders. It also offers suggestions for preventing them. Call 202 783-3238 for the \$1 booklet (order #029-016-00124-7).

■ **CRASH, BANG.** Videonic's Boing Box sound-effects mixer (\$179) lets camcorder filmmakers embellish home movies with 50 noises, including door slams, explosions, and screams.

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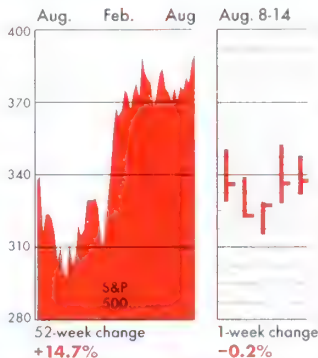
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Investment Figures of the Week

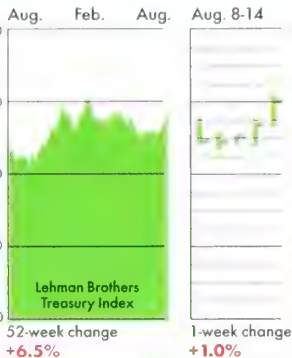
CURRENCY

Don't be under control. That's the wary fixed-income manager included when the July Consumer Price Index came in at a tame 0.2% move up. The market rallied, with the 30-year Treasury reaching levels not seen in months. Short-term interest rates dropped, too. But equity investors chose to focus on the economy. Only small-company stocks and bank stocks, led by the proposed merger of BankAmerica and Security Bancorp, showed much spunk.

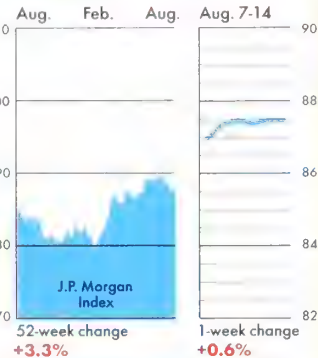
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS	Latest	% change Week	% change 52-week
INDUSTRIALS	3005.4	-13.8	-5.1
COMPANIES (Russell 1000)	204.4	0.1	16.1
COMPANIES (Russell 2000)	174.9	1.0	15.6
COMPANIES (Russell 3000)	217.0	0.2	16.1

INTERNATIONAL STOCKS	Latest	% change (local currency) Week	% change 52-week
FINANCIAL TIMES 100	2608.8	0.4	16.5
NIKKEI INDEX	23,393.3	-1.3	-16.8
TSE COMPOSITE	3541.8	0.4	1.0

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	5.44%	5.53%	7.7%
30-YEAR TREASURY BOND YIELD	8.07%	8.18%	8.8%
S&P 500 DIVIDEND YIELD	3.1%	3.2%	3.4%
S&P 500 PRICE/EARNINGS RATIO	19.9	19.9	15.9

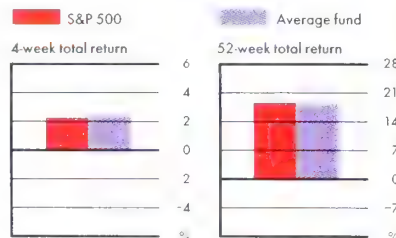
TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 26-week moving average	377.6	376.6	Positive
Stocks above 26-week moving average	53.9%	55.0%	Neutral
Speculative sentiment: Put/call ratio	0.36	0.36	Neutral
Insider sentiment: Vickers sell/buy ratio	2.98	3.32	Negative

INDUSTRY GROUPS

WEEK LEADERS	% change 4-week	% change 52-week	Strongest stock in group	% change 4-week	% change 52-week	Price
USEWARES	15.3	55.8	PREMARK INTERNATIONAL	33.3	69.9	32 1/2
SMETICS	11.6	35.2	GILLETTE	15.2	39.9	41 5/8
PERSONAL LOANS	11.2	41.5	HOUSEHOLD INTERNATIONAL	15.8	51.7	55 3/4
HEALTH CARE SERVICES	9.6	95.7	MANOR CARE	18.2	85.7	22 3/4
REGIONAL BANKS	9.6	44.1	SHAWMUT NATIONAL	60.0	0.0	9
WEEK LAGGARDS	% change 4-week	% change 52-week	Weakest stock in group	% change 4-week	% change 52-week	Price
MINING	-10.7	-30.6	HOMESTAKE MINING	-17.4	-32.0	14 7/8
COMBUSTIBLES	-9.1	-8.3	CHRYSLER	-18.4	-12.3	11 5/8
CHAIN STORES	-7.5	7.5	KROGER	-23.6	27.0	18 1/4
TELECOM	-7.2	2.5	AMAX	-10.4	-13.6	21 1/2
BROADCASTING	-6.1	1.1	COMCAST	-8.3	19.6	13 3/4

MUTUAL FUNDS

WEEK LEADERS	% 4-week total return	% 52-week total return
STRATEGIC INVESTMENTS	11.5	-13.6
STRATEGIC SILVER	10.1	-10.4
UNITED SERVICES GOLD SHARES	9.2	-8.8
WEEK LAGGARDS	% 4-week total return	% 52-week total return
STRATEGIC SILVER	71.3	-33.3
RUSHMORE PRECIOUS METALS INDEX PLUS	68.3	-32.7
STRATEGIC GOLD/MINERALS	63.8	-32.2



RELATIVE PORTFOLIOS

For amounts invested at the present value of \$10,000 one year ago, the relative portfolios show the following day total returns:

U. S. stocks
\$11,777
+1.02%

Treasury bonds
\$11,165
+2.43%

Money market fund
\$10,594
+0.11%

Foreign stocks
\$9,493
+1.21%

Gold
\$9,446
-1.20%

Data on this page are as of market close Wednesday, August 14, 1991, unless otherwise indicated. Industry groups include S&P 500 companies only; performance and share prices are as of market close.

August 13. Mutual fund returns are as of August 9. Relative portfolios are valued as of August 6. A more detailed explanation of this page is available on request.

SALOMON IS NOT TOO BIG TO PUNISH

The \$2.2 trillion market for U.S. Treasury securities is the largest, the most liquid, and probably the cleanest in the world. In the 1980s, markets for other American securities such as stocks, commodities, and junk bonds were plagued by scandals that raised serious questions about their integrity. But until Aug. 9, no serious questions of impropriety had been raised about the Treasury market. On that day, Salomon Brothers Inc., the market's leading player, admitted that in some recent Treasury auctions the firm violated government bidding rules. Then, on Aug. 14, the firm conceded that its top management, including Chairman and CEO John H. Gutfreund, was aware of bidding irregularities in April but failed to take appropriate action.

No charges have been filed against Salomon, but some market participants contend that the firm was trying to manipulate Treasury prices for its own benefit and to the detriment of other dealers (page 54). If the firm is found to have rigged the market, the question becomes what penalties should be imposed. One penalty would be removing Salomon as a primary dealer in Treasury securities. Some contend, however, that Salomon is too big to bar from future auctions. That would undermine the market's liquidity and reduce the government's proceeds from its securities sales, the argument runs.

This reasoning is specious. Barring Salomon would be an extreme step and should not be taken unless the facts point in that direction. Indeed, it would create temporary instability and uncertainty. But eventually, other players would move forcefully to fill the void. After all, the ultimate buyers of these securities are investors, not securities firms.

But there is a much broader reason for cracking down hard on any miscreant, no matter how big and powerful. The perception of the Treasury market's purity is essential. The U.S. needs the market to finance its budget deficits. Treasury securities are owned by central banks throughout the world. The Federal Reserve uses the market to implement monetary policy. If holders of Treasury debt come to believe that the market is rigged and that regulators lack the will to police violations, the results could be catastrophic. The resulting sell-off could push the government's borrowing costs up by billions of dollars. That's why regulators must hack out any abuses in the market and impose appropriate penalties. Let the chips fall where they may.

THE JAPANESE MUST CLEAN THEIR OWN HOUSE

The dark practices that have come to light in Japan are not seen by most Japanese as "corruption." They are institutionalized into the fabric of Japanese society (page 34). That doesn't mean there are no victims. Obvious ones include consumers and small investors in Japan and

competitors overseas. Recently, more and more Japan have come to believe that their entire business system is being handicapped by the negative impression outside Japan.

With the increasing internationalization of Japanese business and finance, traditional ways are clashing with culture of the West. Some embarrassed Japanese even concede that in the eyes of the West, Japanese norms seen as the remnants of the samurai past.

Although anathema to our Western notions of ethics, fairness, corruption Japanese-style seems to strengthen system. By compensating their major clients, for example Japan's Big Four securities firms bolstered the long-term relationships and safety net that create a cozy environment for big business. What would be branded as conflict of interest in America—such as retired bureaucrats joining corporations and ubiquitous gift-giving—helps lubricate the personal relationships so key to the workings of Japanese society.

No one in the West should be lecturing the Japanese how to order their own society. Lately, scandals seem to have become part of the American way of life: insider trading, junk bonds, the S&L debacle, the list runs on. The amount of money, illegality, and venality involved is at least as large as anything seen in Japan. But both cultures have to come to grips with the abuses in their systems if modern trading arrangements are to work effectively.

WHEN BUSINESS SHOULD MIND ITS OWN BUSINESS

In a five o'clock world, when the whistle blows, no one owns a piece of my time," avers the refrain of a 1950s song. But these days, some employers want to tell you what you can do with your time off the job (page 68).

Employers have always been interested in employee off-duty activities to some degree: In the days of the company town, it was common for corporate officials to police their workers' behavior. The meddling of today, however, motivated not so much by morals as by medical costs. In the past three years, corporate insurance plan premiums have risen an average of 17% annually—and employees who engage in unhealthy habits file more claims. Smoking can be hazardous to the company's fiscal health. So some companies are refusing to employ what they deem high-risk types. Many more are introducing disincentives—say, charging these workers extra for their health plan coverage.

Drawing the line between off-hours behavior and on-the-job performance isn't easy. An all-night carousal clearly affects an employee's ability to perform at work the next day. But once you start regulating behavior, where do you stop? What about people who eat lots of greasy foods? What about someone with a family history of heart disease?

And while the share-the-higher-costs argument seems logical, there's little evidence that it really saves money. Companies should, by all means, encourage employees to lead healthier lives. But performance should be the sole criterion for holding a job. Lifestyle discrimination could put companies on a course far more perilous than could tolerating a work force full of smokers and drinkers.

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